

AN EVALUATION OF THE APPRAISAL SYSTEM ON
BRANCH MANAGERS OF THE BANK OF CHINA GROUP

by

CHIU YUN-MING

招潤明

LEUNG KA-CHUN

梁家俊

MBA PROJECT REPORT

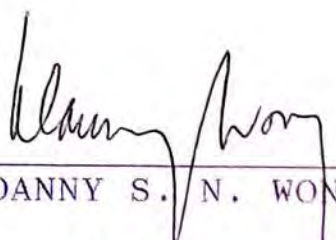
Presented to

The Graduate School

In Partial Fulfilment
of the Requirement for the Degree of
MASTER OF BUSINESS ADMINISTRATION

THREE-YEAR MBA PROGRAMME
THE CHINESE UNIVERSITY OF HONG KONG

May 1991


DR. DANNY S. N. WONG
Advisor

thesis
HG
1615.5
C44

321114



ABSTRACTS

We studied the appraisal system on branch managers of the Bank of China Group and recommended some improvements to increase its effectiveness. Information on the current system were gathered through interviews. Comments and opinion of branch managers were also sought by questionnaires. Base on our analysis, we conclude that the system is unsatisfactory and propose some adaptations to improve its effectiveness.

Among the appraisal factors, the 'branch performance' can be measured quantitatively through an adequate management accounting system. We therefore suggest the introduction of transfer pricing system, the cost and revenue allocation system, the standard cost applications, and the budgetary system into the management accounting system of the Group.

As the changes in the management accounting system require numerous calculations and reportings, it is almost impossible for the Group to implement all the above changes in management accounting system without the use of computer. We therefore also suggest several improvements to the current MIS of the Group.

Finally, to enhance the feasibility of our proposal, we recommend the procedures to be followed by the Group in implementing our suggestions.

TABLE OF CONTENTS

ABSTRACT	ii
TABLE OF CONTENTS	iii
LIST OF EXHIBITS	v
LIST OF APPENDIXES	vi
ACKNOWLEDGEMENTS	vii
CHAPTER	
I. INTRODUCTION	1
The Performance Appraisal	1
The Importance of Appraisal System	2
The Effective Characteristic of the Appraisal System	3
The Problems for an Effective Appraisal System	5
The Significance of the Study	7
Study Object	8
Objective of the Study	10
Target of the Study	11
Scope of the Study	12
Methodology	13
II. THE CURRENT APPRAISAL SYSTEM	17
Bank of China (BOC) Group Background	17
The Organisation Structure of BOC Group	19
Common Methods of Appraisal	29
The Current Appraisal Method in BOC Group	33
The Appraisal Procedures	38
The Final Adjustment Process	40
Limitations of the Current Appraisal System	41
Opinion Research on Branch Manager	43
IV. PROPOSED APPRAISAL SYSTEM FOR BRANCH MANAGER	47
The Basic Framework of the New System	47
The Amendment of the Appraisal Factor	48
The Amendment of the Rating Method of Appraisal Factors	50
The Method of Measurement of Branch Performance	53
The Advantages of the New Appraisal System	63
Problem in Implementing the New System	66

V.	CURRENT BRANCH PERFORMANCE MEASUREMENT METHOD	68
	Availability of Management Information in the Computer Systems	69
	Management Information Not Available in the Current Systems	70
	Description of Current Branch Performance Evaluation Method	72
	Disadvantages of Current Branch Performance Measurement Method	76
VI.	AMENDMENTS OF THE MANAGEMENT ACCOUNTING SYSTEM	81
	Transfer Pricing Analysis	81
	Cost and Revenue Allocation Systems Analysis	90
	Standard Costs Applications	103
	Budget Planning Process	108
	The Branch Profit and Loss Statement under the New Scheme	116
VII.	INTEGRATION OF THE PROPOSED APPRAISAL SYSTEM AND THE CURRENT COMPUTER SYSTEM	119
	Appraisal Factors to be Measured by Computer	119
	Suggestions on the Change of Computer Systems	121
VIII.	RECOMMENDATIONS	123
	APPENDIXES	127
	BIBLIOGRAPHY	143

LIST OF EXHIBITS

EXHIBIT 1	The Organisation Chart of BOC Group	20
EXHIBIT 2	The Organisation Chart of Nanyang Commercial Bank	24
EXHIBIT 3	Managerial Grade Appraisal Form	35
EXHIBIT 4	Weights Check List for Managerial Grade	37
EXHIBIT 5	The Suggested Appraisal Form	54
EXHIBIT 6	Branch Performance Appraisal Form	64
EXHIBIT 7	Branch Profit and Loss Statement	73
EXHIBIT 8	The Cost Flow Sequence in BOC Group	99
EXHIBIT 9	The New Branch Profit and Loss Statement	118

LIST OF APPENDIXES

Appendix 1(a)	Structured Questionnaire for Interview with the Personnel Manager of the Hong Kong and Macau Regional Office	127
Appendix 1(b)	Structured Questionnaire for Interviews with Personnel Managers and Branch Administration Managers	128
Appendix 2	Questionnaire	129
Appendix 3	Structured Questionnaire for Interview with Manager of Accounting Department	131
Appendix 4	Structured Questionnaire for Interview with Manager of System & Method Department	132
Appendix 5	Summary of Results of Questionnaires	134
Appendix 6	Description of the Appraisal Factors of the Managerial Grade	135
Appendix 7	The Current Operation Structure	137

ACKNOWLEDGEMENTS

We acknowledge the supervision and advices of Dr. Danny S. N. Wong. Dr. Wong had provided us with indispensable advices to our research direction and scope of study. His supervision and support led us to finish the project before May 6, 1991.

We sincerely thank Mr. Norman Law, Assistant General Manager of Nanyang Commercial Bank, who gave invaluable help and information on our study.

We are also grateful to all interviewees from member banks of Bank of China Group who discussed with us openly and frankly. Their comments and suggestions are highly appreciated.

Special thanks go to all ladies in our departments who have done most of the typing of our manuscript with great skill.

Most of all, our gratitude and love go to our families. Their support, understanding and encouragement are essential to our completion of this project.

CHAPTER I

INTRODUCTION

The Performance Appraisal

Within any organisation, evaluating others is an inevitable process because we are all working in groups such that we always want to compete with each other and to rate one another in order to seek evidence to uphold our confidence. Such evaluation may be informally existed in any organisation.

The modern management theory has incorporated this evaluating process into the manager's function which is termed as Performance Appraisal. The appraisal process is now concerned with the evaluation of the performance and potential of employees. The process is unavoidable for any manager's daily function because he is always in charge of selecting the right person to do the right job and seeking the right person to whom his duties can be delegated.

The performance appraisal thus attempts to evaluate the individual staff in respect of his success in his present job and potential development for the future. The appraisal process should be a mutual communication between the appraiser and the subordinate so that they can both exchange ideas concerning the performance appraisal and feedback process can be facilitated.

The Importance of Appraisal System

From the wider scope of perspective to study the appraisal system, the purposes of the appraisal process should be accompanied with the total organisational process of providing usable management information for checking the effectiveness of other administrative and managerial procedures.

According to George Thomason¹, there are five objectives in the appraisal process.

1. Improvement of the current performance of the manager on the job through the recognition of current strengths and weaknesses in performance.

¹ George Thomason, A Text of Personnel Management (H.K. Institute of Personnel Management, 4th Ed., 1981) p.304.

2. Guidance of the individual manager on what his strengths and weaknesses in order to construct the most appropriate career path for him.
3. Identification of the stock of trained manpower available for its current needs but also the potential stock for its future development requirement.
4. Improvement of communications within the organisation.

The objectives should be designed to satisfy the needs of the organisation and also those of the individual. Therefore it is important to tailor-made the appraisal system to fulfill the objectives.

The Effective Characteristics of the Appraisal System

An effective appraisal system contains the following characteristics according to George Thomason², K. J. Pasatt³ and Charles M. Ray⁴ :

² George Thomason, A Textbook of Personnel Management (U.K., Institute of Personnel Management, 4th Ed. 1981) p.304.

³ K.J. Paratt and S.G. Bennett, Elements of Personnel Management (U.K., Gee & Co. (Publisher) Ltd.; 1979) pp.96-97.

⁴ Charles M. Ray, Charles L. Eison, Supervision (New York, The Dryden Press, 1983) p.284.

1. The provision of information about existing and potential manpower strengths and weaknesses as a basis for manpower and corporate planning.
2. The indication of which skills need improvement if the performance is to be improved.
3. To provide a basis for determining salary reviews, promotions, transfers, redundancies, dismissals etc.
4. To feedback the information to the employee who is being assessed relating to his performance standard by pointing out his strengths and weaknesses.
5. The stimulation of higher performance, development of potential, and increased job satisfaction.
6. Prioritizing and weighting performance dimensions and performance goals.
7. To appraise the performance precisely, different appraising methods should be adopted according to the characteristics of the performance being measured.
8. To develop suitable appraisal instrument scoring devices and appraisal procedures in order to ensure fair and just appraisals of all employees.

9. To provide a monitoring and auditing processes to ensure proper operation of the system and to identify areas of weakness.
10. To grant employees opportunities for appeal whenever and wherever such action is appropriate.
11. To provide training for all appraisals involved in the appraisal system.

The Problems for an Effective Appraisal System

The previous section has discussed a lot of ingredients of an effective appraisal system. However, a lot of problems need to be solved before such system can be fully implemented.

1. The most critical step in any appraisal system is to define performance with a precise definition of the components in good performance. Otherwise, we cannot develop a system to distinguish good performance from poor performance.
2. There is no agreement on the employee's expected results and performance between the appraiser and the subordinate. Thus subjective measurement may arise and initiate conflicts.

3. Even if standard of performance has been set, there is no ongoing review of the situation so that the standard may be outdated. Without any adjustment beforehand, the appraisal system is still ineffective.
4. Because the actual performance cannot be accurately appraised, the employee does not feel that there is strong correlation between the reward and performance level. Thus, the motivational effect in the appraisal will become very weak.
5. All performance appraisal systems are subject to certain errors.

Unreal consistency may be a popular error found in rating system. A person may be rated high on all dimensions of performance due to a very outstanding performance on one or two dimensions.

Central tendency is also a common problem where appraiser may have a central tendency to rate the individual average on all dimensions even variation exists in fact.

Different rating may be given to the same employee on the same dimension due to the dissimilarities in perception by different appraisers (if such factor

cannot be quantified).

6. Rating subordinates would be very time consuming and unpleasant task if the rating system is complex and involved many subjective judgment. Appraiser may find that giving honest, comprehensive appraisal to subordinates not only wasting his time but also creating negative relationship with subordinates. To solve the issue, managers may attempt to rate everyone the same and everyone high.
7. The appraiser may not have many opportunities for observing the performance of the employee. Thus, it is very difficult for the appraiser to rely on his subjective judgment to perform the appraisal.

The Significance of the Study

Since many writers had mentioned the importance of the appraisal system in the management process and its significant contribution in the management information system, management should have great interest to know how to set up an effective appraisal system and overcome the aforesaid problems. Thus, we try to make a thorough study on this issue and proposed a new system for the study object. Through this illustration, we hope the management can gain an insight into the effective appraisal system.

Study Object

Hong Kong is one of the major financial centers in the Asian Pacific region. The banking industry has contributed a lot on this development. Due to its important role in Hong Kong, it is worthwhile for us to concentrate our study on this industry.

To confine our study object, we proposed to study the Bank of China (BOC) Group concerning our issue. There are several reasons we have considered to support our choice.

1. BOC Group has grown up prominently since 1979 when all the group members jointed together to share common computer resources. Nowadays, it becomes the second largest bank group in Hong Kong. In term of total assets market share (in all currencies), it occupied 8 percent⁵ at the end of 1989; in term of HK\$ deposits it occupied 21 percent⁶, amounting to HK\$960 billion at the end of 1989. Thus, the Group has a significant influence upon the Hong Kong Banking sector.

⁵ Annual Report 1989, Commissioner of Banking, p.32.

⁶ Annual Report 1989, Commissioner of Banking, p.33.

Moreover, BOC Group is one of the largest retail bankings in Hong Kong. The total number of branches at the end of 1989 is 313⁷, which represents 23 percent⁸ of total branches of licensed banks in Hong Kong. The total number of employees in the Group is around fourteen thousand at the end of 1989, which is 21 percent⁹ of total employees of licensed banks in Hong Kong. Thus, the Group should be a representative example in analyzing the managerial problems of appraisal system in Banking industry.

2. The BOC Group is now taking more responsibility in the financial industry development in Hong Kong. The recent change of domicile of the Hong Kong Bank and the issue of 1997 have made BOC Group to become a quasi-central Bank in Hong Kong. No doubt that she will play a more active role in Hong Kong. Therefore, her future development in the management philosophy may have material effect upon Hong Kong's future. Our study may be one of the forward steps to look into this matter.

⁷ Huang Diyan , "Bank of China Group and Hong Kong and Macau's Economy Prosper Simultaneously" Study of International Finance (Beijing), May 1990, p.33.

⁸ Annual Report 1989, Commissioner of Banking. p.62.

⁹ Ibid. p.92.

3. From the recent changes in BOC Group business strategies such as active participation in syndicated loan market, foreign exchange market and housing mortgage, renovation of bank premises, employment of professionals, computerization of banking services etc., all reveal that the BOC Group has experienced a tremendous changes in organisation structure, management style, organisation behaviour, and management information system. Based on our intuition, we do believe such situation would provide us a lot of opportunities to explore the managerial problems which are worthy of recommendations.

Objective of the Study

The two objectives of our study are shown as follows:

1. To make recommendation for the existing appraisal system so that a prominent relationship between performance and reward can be perceived by the staff.
2. To improve the management accounting system to the extent that staff performance can be measured for purposes of analysis, decision making and control.

Target of the Study

To have a concrete plan to achieve our objectives, we identify the following targets:

1. To understand the current appraisal system implemented by the Group.
2. To analyze the assessment method on the performance of staff and how such data is gathered, classified and reported to the management.
3. To identify the weaknesses and drawbacks of the current appraisal system and problems encountered by the management in improving the system.
4. To suggest alternatives to improve the performance appraisal system.
5. To evaluate the existing management accounting system in respect of the information concerning the performance of staff, the planning and control action, the optimization of resource applications.
6. To suggest directions for the future development of the management accounting system.

7. To design an effective approach to consolidate the management accounting system and the appraisal system so that staff can perceive performance and appraisal positively correlated.

Scope of the Study

A bank's usual structure can be divided into four areas:-

Branch

Department

Back office

Subsidiary

Since the tasks and objectives of each area may have much differences and require separate approaches to appraise their performances, it is beneficial to concentrate our study on the branch area in order to optimize the benefits envisaged with our limited time and resources.

Because BOC Group places great emphasis on the retail banking business which contributes the major sources of profit, the scope of this study is confined to the branch managerial level who are responsible for the profitability of branches.

By improving the performance at the branch managerial level, the Group can sharpen its front line competitive edges and enhance its profitability.

Methodology

Being a well-known banking group in Hong Kong, all member banks of the BOC Group have the same appraisal system. In order to minimize our time in finding out the mechanism of the existing appraisal system, we interviewed the personnel manager of the Hong Kong and Macau Regional Office of the Group¹⁰. The personnel managers and managers of branch administration division of four selected banks were interviewed. The interviews are aimed at learning their understanding, experience and attitudes on the following issues:

1. Problems and difficulties encountered in carrying out the appraisal
2. General responses from the staff on the appraisal system

¹⁰ Readers may refer to the section "The Organisation Structure of BOC Group" in Chapter III on p.20 for detailed explanation of the Regional Office's functions.

3. Comments on the appraisal system

4. Suggestions on improvement

In order to ensure that we covered all the major issues, we used structured questionnaires in our interviews. The questionnaire is shown in Appendix 1. All interviews were carried out in bank premises. Interviewees were encouraged to give their comments and opinions on the issues by promising them that their identities would be kept anonymous.

Sixty questionnaires were sent out to branch managers through personnel departments of member banks. Respondents were requested to send back the questionnaire to us directly within ten days. We received 42 responds totally. The questionnaire, which is shown in Appendix 2, aims at finding out the responds and attitudes of branch managers on the following areas:

1. The effectiveness of the current appraisal system
2. The constraints affecting the branch managers' performance

3. The adequacy of current management information system (MIS)
4. Suggestions on improvement of appraisal system

With the help of Nanyang Commercial Bank, we have a more detailed study on the branch performance measurement method and the current computer systems. In addition to reviewing the relevant documents such as system manuals and accounting manual, we interviewed with the manager of the Accounting Department and the manager of the System and Method Department. Once again, structured questionnaires shown in Appendix 3 and 4 are employed to ensure the major areas of discussion being covered. The areas of discussion in branch performance measurement method includes:

1. General understanding of the method
2. Reports generated for the measurement
3. Problems and difficulties encountered
4. Areas of improvement

The areas of discussion in computer systems include:

1. General understanding of all systems
2. Relation between different applications
3. Adequacy of management information provided
4. Problem in the current systems
5. Areas for improvement

Problem areas are identified after thorough studies on the appraisal system, the branch performance measurement method, and the MIS. With the insights from relevant books and periodicals, we develop our suggestions on improvements.

Lastly, we estimate the difficulties in the implementation.

CHAPTER II

THE CURRENT APPRAISAL SYSTEM

Bank of China Group Background

Bank of China

Bank of China was formed in 1908 and is the oldest Chinese banking institution still functioning. It is now China's specialized foreign exchange bank. Its Hong Kong branch was established long time ago. It has high prestige and great influence on the banking sector.

Bank of China Group

There are 14 member banks in the Bank of China Group. Only one of them, Bank of China, Macau, is carrying on business in Macau. Other member banks are carrying on business in Hong Kong. Among the 13 banks, four of them are locally incorporated while the other nine are China-incorporated. The four locally based banks are Nanyang Commercial Bank, Po Sang Bank, Hua Chiao Commercial Bank and Chiyu Banking Corporation. The nine China-incorporated

banks are Bank of China, Bank of Communications, Sin Hua Trust Savings and Commercial Bank, The Kwangtung Provincial Bank, Kincheng Banking Corporation, The National Commercial Bank, The China State Bank, The China & South Sea Bank, The Yien Yieh Commercial Bank.

Like Bank of China, all member banks have established their branches in Hong Kong for a rather long time. Besides, they all have Chinese capital and most of their businesses are related to China.

Development History

Since all members banks have similar backgrounds and areas of business, they have frequent contacts among themselves. In the late 70s, members were forced to cooperate more closely to cope with the fierce competition from other banks in Hong Kong. With the introduction of computer in the Hong Kong banking industry, the member banks had to use the expensive but effective computer resources to survive. In order to share the valuable computer resources and to achieve economy of scale, members found that they should share the same computer resources and should formally join together to enlarge their branch networks. Therefore BOC Group emerged.

Objectives of the BOC Group

At the beginning, the Group's most important task is to offer contributions in terms of foreign exchange and provide funding to support China's Four Modernization Plan.

After the signing of Sino-British Agreement, the Group are making efforts to promote the prosperity and stability of Hong Kong and also to promote the economic contacts between Hong Kong and China.

The Organisation Structure of BOC Group

(1) The Role of the Hong Kong & Macau Regional Office

Referring to the Exhibit 1, the 14 member banks, the EDP center and the training center are under the direct control of the Hong Kong and Macau Regional Office (Regional Office).

All member banks lied on the same hierarchy and no one bank can rule over the other.

The Group controller is the Bank of China, Beijing, the Head Office of the Bank of China. However, the daily control procedures are implemented by the Regional Office.

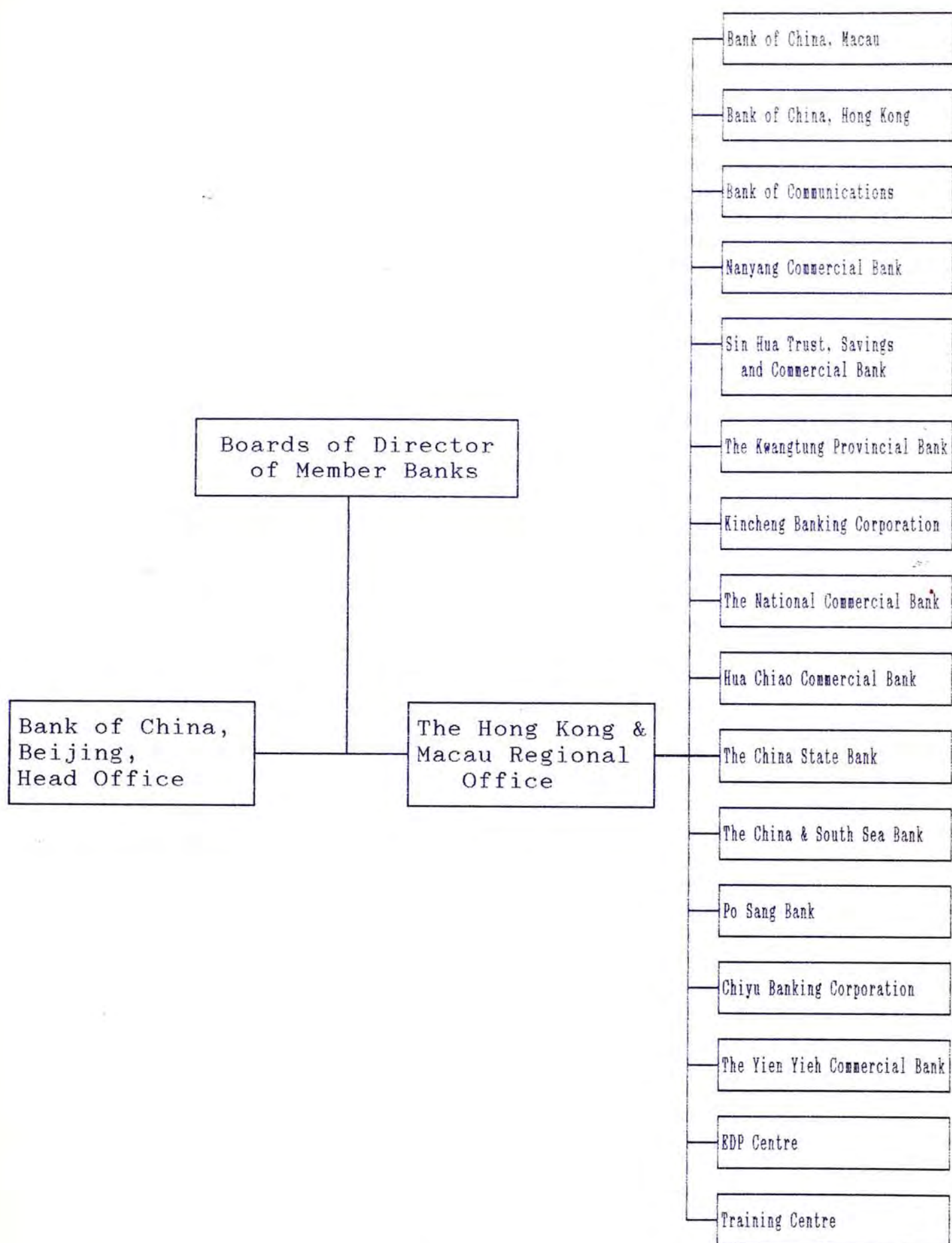


Exhibit 1. The Organisation Chart of Bank of China Group

The Regional Office is vested with the authority to lead, manage, coordinate and control the operations of member banks and the two supporting centers from the Head Office of BOC. It also acts on behalf of member banks' Board of Directors to discharge their duties.

The control procedures include standardisation of procedures, management information reports, management audit, mainframe control and moral suasion. Material group decisions are left to the Regional Office to decide and members are obliged to follow the rules of the game.

(2) The Interrelationship between Member Banks

Two approaches are followed to study this aspect :

Areas decided independently by each bank.

1. The Internal Management Policies

For example: The credit approval procedures even though the Regional Office may set some guidelines for member banks to follow.

2. Product Innovation

For examples: BCU in Bank of China and
USD mortgage loan in Po Sang Bank
even though most of the
traditional products are
standardised.

3. Market Image

For examples: Banker for Industrial Loan: Sin
Hua Bank
Banker for Bullion Trading: Po
Sang Bank
even though the BOC Group sharing
same strategic objectives.

Areas common for all member banks:

1. They are sharing the same mainframe computer so that most of the operational procedures are standardised by software applications.
2. The interest rate pricing, and foreign exchange spread are standardised for all member banks to reduce intergroup competition.

3. Each member bank has to act as an agent on behalf of other members to handle their customers' retail banking transactions such as deposit/withdrawal of saving and current account, bullion trading, credit card application and sale of traveler's cheque.
4. Same reward system is implemented such as salary scale, bonus scheme, fringe benefits and welfare to eliminate the human resources competition within the group.
5. Organisation structure and design are similar to facilitate the Regional Office to implement the strategic policies, the control procedures, and standardisation of communication network.

(3) The Organisation of a Member Bank

Nanyang Commercial Bank (NCB) is chosen to illustrate the typical organisation structure of the BOC Group. An adapted version of NCB organisation structure is shown in Exhibit 2.

The organisation structure can be roughly divided into four sectors. The top management is responsible to the Board of Directors, in other words, to the Regional Office.

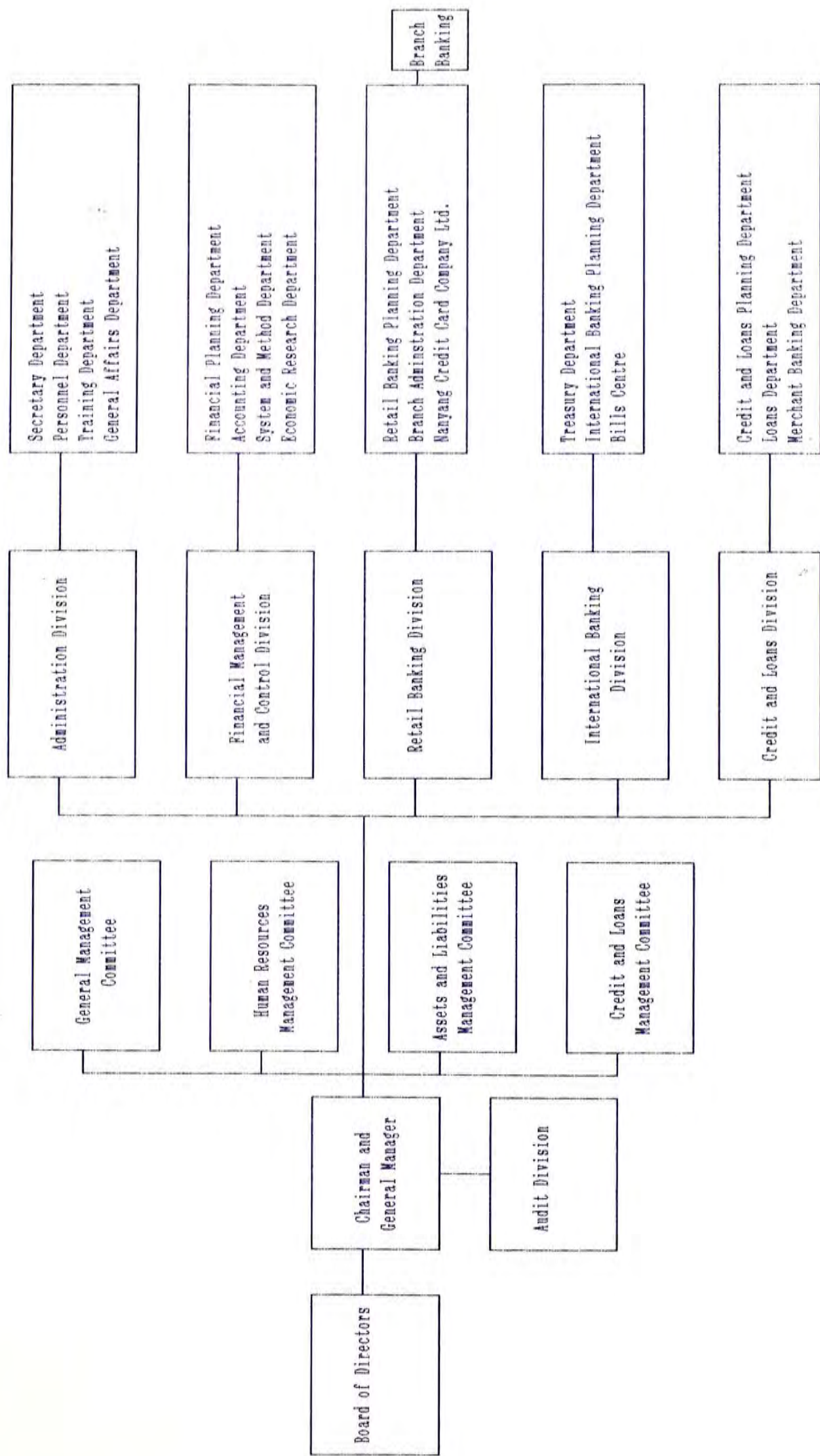


Exhibit 2. The Organisation Structure of Nanyang Commercial Bank

Source : Adapted from Annual Report 1989,
Nanyang Commercial Bank.

Then there are four committees acting as the think-tank to assist the top management to make decision and develop internal policies. Members in these think-tanks are composed of the Division heads.

Divisions execute and monitor the policies and related activities according to the task nature.

1. Administration Division: responsible for the administrative tasks such as personnel function.
2. Financial Management and Control Division : responsible for the financial matters and system control such as accounting and organisation & method functions.
3. Retail Banking Division: responsible for the development of business such as branch banking and credit card business.
4. International Banking Division : responsible for interbank businesses such as treasury function and bills business.

5. Credit and Loans : responsible for loans
Division administration and credit
control and to handle
specialised loan proposals.

Under each division, there are several departments to implement the tasks. With an exception, under the Branch Administration Department, the Branch Banking is the further extension of this Department which represents the major force in the retail banking business.

There are several types of departments found in BOC Group. The two most common ones are profit center and cost center. According to the organisation design of NCB, departments in the Administration Division and the Financial Management and Control Division are classified as cost centers which provide supporting services for the profit centers to operate efficiently and effectively.

For the remaining three divisions, there is at least one department classified as profit center such as the Branch Banking, Treasury Department and Merchant Banking Department.

1. Branch Banking : making profit from the retail
business such as housing mortgage,
small business loans and taking
deposit from customers to provide
funding for other profit centers.

2. Treasury : making profit by placing the excess
Department funds (not being used by the Branch
Banking and Merchant Banking
Department) into the interbank
market.
3. Merchant Banking : making profit by arranging
Department syndicated loan as lead manager or
participating into syndicated loans
as panel member.
4. Credit Card : a typical type of subsidiary
Company company providing credit card
services which is responsible for
its own profit and loss.

Each of these profit-making divisions has a strategic planning department or an operation center to provide specialised services to facilitate the business operations.

1. Retail Banking : responsible for the innovation and
Planning development of new retail products
Department or services.
2. Branch : responsible for the development and
Administration coordination of the Branch Banking
Department business.

3. International Banking Planning Department : responsible for the monitoring and analysis of the interbank business which also includes the bills business.
4. Bills Center : responsible for the technical operations of the bills business.
5. Credit and Loans Planning Department : responsible for the analysis of the loans business operations and related products development.
6. Loans Department : responsible for the technical operations of the loans business.

Not all member banks provide the aforesaid specialised departments in their organisation structures. However, the functions for these specialised departments may be incorporated into the profit center and cannot be differentiated simply by using the organisation chart shown.

Moreover, NCB defines Bills Center and Loans Department as operation centers which serve solely for profit centers on piecemeal basis in order to distinguish their nature with those of cost centers which provide general services to all departments and branches.

Common Methods of Appraisal

The basic goal of performance appraisal is to evaluate the past performance of the employee. The common method is to compare employee's performance against each other. The most suitable person to act as the appraiser (or rater) is usually the immediate boss of the subordinate.

However, most of the appraisal methods are very subjective approaches and the overall impression of the subordinate will be easily influenced by one or two prominent past events.

According to Mitchell S. Norit¹¹, there are some basic tools of appraisal methods commonly used in the business world.

1. Straight Ranking

- i. Ranking all the members of a group from best to poorest

¹¹ Mitchell S. Novit, Essentials of Personnel Management (U.S. Prentice-Hall Inc. 1979). pp.143-144.

ii. Done on some subjective global dimension of performance

iii. Advantages:

a. simple

b. ranking according to each group of candidates' characteristics

iv. Disadvantages:

a. Difficult to apply when a lot of subordinates involved

b. Ranking may not conform to a normal distribution from high to low

c. Difficult to compare one group with another

2. Forced Distribution

i. The appraiser are required to distribute staff into a fixed number of categories such as excellent, above average, average, below average and poor.

- ii. The percentage of the group to be placed in each category has been pre-determined by the personnel and may be applied on global basis.

- iii. Advantages

- a. Avoids tendency of the appraiser to rate the majority staff into one or two types of categories
- b. Reduces central tendency
- c. Effective for large group of candidates

- iv. Disadvantages

- a. Inflexible to distribute the rank to candidate even though their performances entitle to such rank
- b. Seldom have specification of the basis for placing persons in various categories

3. Conventional Scale Rating

- i. The appraiser is given a form for each employee to be appraised.

ii. The form lists a number of factors or characteristics against each of which is scale.

iii. The appraiser is required to indicate his assessment of the employee by rating his performance against the factors or characteristic.

iv. Advantages

- a. Simple to develop and install
- b. Systematic way (standard form) for appraiser to perform assessment
- c. Provide some information for developmental feedback because employee can check his result of the rating against performance standard
- d. Do not rely on the ability of the appraiser to express his comment in writing

v. Disadvantages

- a. Vulnerable to the error of unreal consistency which the appraisers are likely

to average the employee's evaluations for individual factors to get an 'expected' rating

- b. The rating factors or characteristics may not be relevant to the employee's performance
- c. The dimensions of such factors or characteristics are rarely well defined and thus allow the appraiser to apply his own definition which may lead to subjective approach
- d. Some of the factors may overlap if they are not well defined and lead to difficulties in assessment.

The Current Appraisal Method in BOC Group

The current appraisal method adopted by BOC Group is in fact a combination of the three basic tools mentioned previously.

An appraisal form is designed for employees and appraisers to fill in. The form is similar to that of conventional scale rating method whereas there are several appraisal factors which both parties have to rate. The detail of the appraisal form is shown in Exhibit 3 which is slightly adapted for illustration purpose.

The illustrated form is designed for managerial grade. There are ten appraisal factors which are regarded as relevant to the performance of a manager. The explanation of each appraisal factor is shown in Appendix 6.

In addition, there are four types of appraisal forms designed for different grades of employees. The non-skilled grade, clerical grade, and officer grade have to fill in specific form solely for individual group. Each type of form have different appraisal factors according to their nature of duties. However, they are out of our study scope, the illustrations of their appraisal form are skipped.

For the same managerial level, different task natures or responsibilities are assigned to manager according to his department's function or his role in that department. For example, the manager of a profit center may place more emphasis on business achievement than that of a back office manager.

Item	Score	Excellent	Good		Average		Satisfactory		Poor	Self Evaluation	First Appraiser	Second Appraiser	Final Appraiser	Weight	Weighted Score
		8	7	6	5	4	3	2	1						
Business Achievement			X										7	2	14
Leadership Skill		X											8	1	8
Business Knowledge			X										7	1.5	10.5
Analytical and Judicious Ability			X										7	1	7
Training Skill			X										7	1	7
External Relationship		X											8	1.5	12
Innovative Ability			X										7	1	7
Sense of Responsibility			X										7	1	7
Personal Conduct and Behaviour			X										7	1.5	10.5
Interpersonal Relationship			X										7	1	7
Grand Total														12.5	90

Exhibit 3. Managerial Grade Appraisal Form

Source: Adapted from Nanayang Commercial Bank

To adjust for this difference, the factors are weighted for different scoring scale. There is a check list of weights (refer to Exhibit 4) for the appraiser to assign numerical weights to each factor in order to show the importance of each factor towards individual's performance standard. Thus, the profit center manager may have more weighting upon certain factors such as business achievement and external relationship but the back office manager may have more weighting upon other factors such as analytical and judicious ability, and innovative ability.

The appraiser is required to indicate on each scale his assessment of the employee in respect of that appraisal factor. The numerical value of the scale selected represents the score of the factor under consideration.

Function Weights Item	Manager of Staff function department	Manager of Branch	Marketing Manager	General Affairs Manager
Business Achievement	1	2	1.5	1
Leadership Skill	1	1	1	1.5
Business Knowledge	1.5	1.5	1	1
Analytical and Judicious Ability	1.5	1	1.5	1
Training Skill	1	1	0.5	1
External Relationship	1	1.5	2	1.5
Innovative Ability	1.5	1	1	1.5
Sense of Responsibility	1.5	1	1.5	1.5
Personal Conduct and Behaviour	1.5	1.5	1.5	1.5
Interpersonal Relationship	1	1	1	1
Grand Total	12.5	12.5	12.5	12.5

Exhibit 4. Weights Check List for Managerial Grade

Source: Adapted from Nanayang Commercial Bank

The numerical score is multiplied by the predetermined weights shown on the check list to arrive at the weighted appraisal factor score. Adding up the weighted scores provides a grand total which represents the ranking score of the employee.

An illustration on how to arrive at the grand total is shown in Exhibit 3.

The Appraisal Procedures

1. The form is first filled in by the employee himself.
2. He evaluates himself against each factor.
3. His own rating acts as a reference for appraisers.
4. Moreover, he can add some narratives to describe his performance in order to enrich the information given to the appraiser.
5. Usually, the appraiser is the immediate supervisor. Before the appraiser decides the score, an interview will be conducted between the employee and the appraiser so that the rating will be more objective and provide an opportunity for them to communicate frankly.

6. Then the appraiser will choose the appropriate score for each factor or characteristic and foot up the grand total. The appraiser may also add some narratives to support his ratings.
7. For those appraisers with lower rank, the immediate boss of the appraiser acts as the second appraiser in order to avoid biased or subjective rating. The division head or department head collects all his subordinates' appraisal forms and take an overall review. Then he may add the final comment of the rating of the subordinates.
8. Using the straight ranking method, he ranks all the members of the group from first to last. According to this ranking, the head should determine the grading of each staff by classifying them into categories of excellent, good, average, satisfactory, and poor. The classification is similar to that of forced distribution but there is no pre-determined percentage for such classification.
9. Finally, the forms are sent to the Personnel Department for the corporate adjustment and will form the reward distribution basis. A more important effect is that such ranking will be the essential evidence for staff promotion, salary review, etc.

The Final Adjustment Process

The Personnel Department receives all the appraisal forms and examines all the details including footing, narratives, comments, departmental grading etc. It will adjust the mean score of each department / division to the corporate mean score by an adjustment factor. Thus, each individual's grand total score will be adjusted by this factor in order to arrive at an adjusted score.

The Personnel Department will make use of this adjusted score to assign the staff into the grading categories in accordance with predetermined percentages which are decided by the Regional Office. The method is similar to the Forced Distribution Appraisal Method described in the previous section 'Common Methods of Appraisal'.

The grading results compiled by the Personnel Department may not match that graded by the Department / Division head. Before the grading is finalised, a review by the Department/Division head will be arranged so that they can give their final comments on it. Any change of grading should be supported by narratives written by the department head. However, the final decision still rests with the head of Personnel Department.

Limitations on the Current Appraisal System

Based on the research study made on branch managers and data gathered from the interviews, some major limitations can be concluded.

1. There are no quantitative measurement for the appraisal factor especially related to the business achievement factors.
2. As BOC Group does not have a elaborate system for budgeting, there are no well defined yardstick to measure performance. Therefore, the branch manager does not know how well his work has been performed even though his rating may be relatively high.
3. Since there is no channel provided for the manager to participate in setting the performance standard and no standard has been announced, he does not know what level of performance is expected from him.
4. Without objective measurement yardsticks, the system cannot eliminate personal bias in rating an employee if it relies on his immediate boss's final judgment.

5. The branch manager does not receive sufficient feedback on his performance. In fact, what he knows is only the final grade with few comments from his immediate boss.
6. Since the rating is based on limited personal judgment, the branch manager cannot receive sufficient evident and feedback from other related scope. Therefore sources of information to improve his performance is restricted.
7. Some of the appraisal factors may not be relevant to the branch manager's performance. On the other hand, some relevant factors may be missed.
8. Some appraisal factors may not be well defined which may lead to ambiguity when these factors are rated against the manager's performance.
9. The current MIS cannot provide sufficient data to reflect the branch manager's performance. Thus, the incorporation of data from the current MIS to the appraisal system seems to be ineffective.
10. The appraisal system has no motivational effect upon the branch manager's performance.

Opinion Research on Branch Manager

Forty-two out of the sixty issued questionnaires were returned from the respondents. The sample represents 13.4 percent of the population. The aim of the questionnaire is to find out the general opinion of branch managers on the current appraisal system and the current computer system. We also identify factors that branch managers disagree to take into consideration in their own appraisals. Opinion on the effectiveness of the MIS are sought. Finally, an open-ended question was used to gather suggestions on improving the appraisal system.

Means and distributions of responses of the closed-end question indicate the opinion and preference of branch managers. The results are summarized in Appendix 5.

We found that the existing appraisal system is not an effective one but it affects rewards of branch managers. Branch managers are not involved in selecting the factors to be measured in their appraisal. Therefore, they believe the appraisal factors are insufficient and inappropriate. Without an appropriate measurement, the system cannot find out strengths and weaknesses of branch managers. Moreover, as there is no quantitative measurement, the appraisal result depends on the subjective

judgment of appraiser. Based on the above analysis, branch managers believe their bosses do not know their exact performance. In the existing appraisal system, appraisers are not required to give feedback to subordinate so branch managers do not know their problems from the appraisers' point of view. Thus they cannot improve themselves to meet the performance requirements.

We also found that branch managers object to taking the followings as a measurement factor:

1. Allocated cost - inappropriate allocation basis
2. Shared revenue - inappropriate sharing basis
3. Personnel costs - salary is determined by personnel department
4. Budgetary control - no complete system
5. Branch Location - not selected by branch manager

Branch manager generally admit that the factor under their control should be measured in the appraisal and all uncontrollable factors should not be measured. Besides, allocated revenue and expenses should have equitable and fair bases of allocation and the bases should be agreed by branch managers.

For the current MIS, we found that it is totally unsatisfactory in respect of providing appraisal information. The system cannot provide true operating costs of branches, data to carry out responsibility accounting system, data to help branch managers to make decision, and information on branch manager's performances. The results indicate that we should have a study of the current computer system and make recommendations to improve the current situation.

Branch managers suggest that a more quantitative approach in appraisal is more desirable. Furthermore, they want more involvement in setting the performance standard. Feedbacks from appraisers are also strongly requested by branch managers.

In the interviews with managers of Personnel Department, we find that they think the current appraisal system is an effective one. Not only because it is a common appraisal method but also there have not been many complaints received since its employment five years ago. However, they admit that even the appraisal results affect the rewards and promotion, staff who are affected by the organisation culture of BOC Groups seem to accept this kind of appraisal system. Now, they have no plan to change the current appraised system but they will change if feasible and reasonable recommendations are available.

In the interviews with managers of Branch Administration Department, the interviewees disclose the major difficulties in the appraisal are the interpretation of factors, the decision to assign score, insufficient information on performance of branch managers. The overall impression is that the appraisers do not have a good yardstick in assessing the performance. They incorporate much subjective judgment and rely on one or two significant instants to infer the overall impression on the employees.

From the above analysis, we conclude that the existing appraisal system is unsatisfactory for both appraisers and subordinates. We propose some adaptations on the current system to improve its effectiveness. The proposal will be discussed in the next chapter.

CHAPTER III

PROPOSED APPRAISAL SYSTEM

FOR BRANCH MANAGER

The study of the current system reveals several weaknesses which may demotivate branch managers' performance. In order to eliminate or at least to reduce the effect of the loopholes in the system, a new design for the appraisal system at the branch manager level of BOC Group is recommended.

The Basic Framework of the New System

Conventional scale rating will still be applicable due to its popularity in BOC Group and its systematic measurement.

Since the branch managers' performance probably can be reflected in the branch performance, the 'branch performance' factor should be incorporated into the appraisal list in order to link up manager's performance and the appraisal result. As branch performance can be

measured quantitatively, it provides an objective measurement for branch manager.

To reduce ambiguity of the appraisal factors, some of them may be eliminated or modified so that more objective measurements can be adopted.

To place more emphasis on certain appraisal factors in order to enhance their importance relating to the manager's performance, the original check list of weights may also be modified.

To avoid subjective rating by the immediate boss, the new system may rely heavily on peer review and subordinate review.

The Amendment of the Appraisal Factor

For readers to understand the following sections easily, you may refer to Appendix 6 for detailed description of each appraisal factor. 'Business achievement', 'analytical and judicious ability', and 'external relationship' can be combined and measured by the 'branch performance' factor because these factors can all be correlated with the branch performance.

'Personal conduct and behaviour' should be eliminated because it is too subjective for measurement and it does not have hard and fast rule to determine the rating.

Adding a 'problem loan ratio' to measure the ability of branch manager in handling problem loan accounts in the past three years. Problem loan is defined as the loan for which specific provision for bad debt has already been made. Branch managers are held responsible for these loans. Once a manager assumes responsibility on the problem loan, such loan balance will exist in this factor unless the problem loan has been settled or written off (3 year after the loan began illiquid). The objective of this ratio is to avoid the case that the manager may discharge his liability if he has been transferred to another branch. This problem loan balance will still be appended to his appraisal factor.

The measurement of problem loan ratio is by calculating the following ratio:

$$\frac{\text{Problem loans that the branch manager was responsible for in the past 3 year}}{\text{Total loans recommended by the branch manager in the past 3 year}} \times 100\%$$

If the branch manager controls his loan quality, the amount of problem loans may decrease and the ratio could approach to zero. Since the ratio has retrospective effect, the branch manager must take a constant review on

the loan portfolio's quality and should not just aim at the loan size.

The Amendment of the Rating Method
of Appraisal Factors

The business knowledge will be measured by the following three factors:

1. The level of education and any further professional training.

The scores will be allocated as follows

i. Secondary 5	2 points
ii. Secondary 7	3 points
iii. Post Secondary qualification other than degree	4 points
iv. Degree	5 points

For any further qualification obtained, such as MBA, ACCA, one more point will be added to the basic score. Maximum score for this factor is ten.

The aim is to motivate the manager to obtain further qualification in order to enrich his business knowledge in academic and professional field.

2. The number of years of banking experience

For every two years banking experience one point will be counted. Maximum score for experience is five. The experience should be counted from the time when the branch manager had taken up his current post.

The aim is to relate the branch manager's experience to the business knowledge. However, when the branch managers have more than ten years experience, no more point will be added because there is not much difference in business knowledge level between managers with ten year experience and those with over ten years experience.

3. The number of training courses attended by the branch manager.

For each calender year branch manager will be encouraged to attend training courses such as those held by the Training Center or other professional bodies. Every course (which should be approved by the Personnel Department) they have completed will be counted as one point. Again, the maximum score for this factor is five points.

The aim is to encourage the branch manager to update his professional knowledge and to widen his scope of knowledge.

The final score of business knowledge will be computed by adding the total score from these three items and then divided by 20 and multiplied by 8.

The leadership skill and training skill should be measured by the branch manager's immediate boss and his immediate sub-managers and officers.

The aim is to assess the branch manager's skill from various concerned parties so as to obtain more objective judgment. The final score will be the average of these three parties' scores.

The innovative ability should be evaluated by the branch manager's immediate boss and the Retail Banking Planning Department head because they have a lot of chance to assess manager's innovative ability in their daily contacts. The final scores will be the average of the two parties' scores.

The sense of responsibility is still rated by the manager's immediate boss. The boss should be the most suitable person to justify this factor because he is the

sole person to delegate his authority to the manager. To make this rating more objective brief explanation will be required to support the score.

The interpersonal relationship should be measured by the manager's colleagues who are usually managers of other branches. Three branch managers will be chosen by the Personnel Department randomly to perform this assessment. They need to give a brief explanation for their assessments. The final score is the average of their scores.

A newly designed form is shown in Exhibit 5.

The Method of Measurement of Branch Performance

To be a fair measurement of branch performance, a standard of performance should be set up and the actual performance should be compared with such standard. Achieving the standard will be regarded as reaching the average level of performance.

Two levels of standard will be employed to measure against the actual branch performance.

Branch Manager Appraisal Form

Score Items	Excellent	Good		Average		Satisfactory		Poor	Reference	W e i g h t	Weighted Score	Self Eva- uation
	8	7	6	5	4	3	2	1				
Branch Performance	over 130%	130%-121%	120%-111%	110%-101%	100%-91%	90%-81%	80%-71%	70% or below	Refer to Appended Sheet			
Business Knowledge	Pts=8	Pts=7.9 to 7	Pts=6.9 to 6	Pts=5.9 to 5	Pts=4.9 to 4	Pts=3.9 to 2	Pts=1.9 to 1	Pts=0.9 to 0	Education = Experience= Training course = _____ Total = _____ Point=(Totalx8)/20			
Leadership Skill	Pts=8	Pts=7.9 to 7	Pts=6.9 to 6	Pts=5.9 to 5	Pts=4.9 to 4	Pts=3.9 to 2	Pts=1.9 to 1	Pts=0.9 to 0	Boss = Sub-mgr = Officer = _____ Total = _____ Point = Total/3			
Training Skill	Pts=8	Pts=7.9 to 7	Pts=6.9 to 6	Pts=5.9 to 5	Pts=4.9 to 4	Pts=3.9 to 2	Pts=1.9 to 1	Pts=0.9 to 0	Boss = Sub-mgr = Officer = _____ Total = _____ Point = Total/3			
Innovative Ability	Pts=8	Pts=7.9 to 7	Pts=6.9 to 6	Pts=5.9 to 5	Pts=4.9 to 4	Pts=3.9 to 2	Pts=1.9 to 1	Pts=0.9 to 0	Boss = Retail Planning= _____ Total = _____ Point = Total/2			
Sense of Responsibility									Remarks:			
Interpersonal Relationship	Pts=8	Pts=7.9 to 7	Pts=6.9 to 6	Pts=5.9 to 5	Pts=4.9 to 4	Pts=3.9 to 2	Pts=1.9 to 1	Pts=0.9 to 0	Mgr 1 = Mgr 2 = Mgr 3 = _____ Total = _____ Point = Total/3			
Problem Loan Ratio	1% or Below	1.1%-2%	2.1%-3%	3.1%-5%	5.1%-7%	7.1%-10%	10%-13%	13% or above	Problem Loan Total Loan			
Grand Total												

Exhibit 5. The Suggested Appraisal Form

1. The objective of the branch which can be measured quantitatively should be the attainable profit level of the branch. The profit is defined as the net profit¹² after the deduction of all the controllable costs¹³ but before the deduction of uncontrollable cost¹⁴. Thus, the manager is fully responsible for the budgeted profit. Any variance from the budget should be explained by the manager.
2. In addition to branch objective measurement, several targets should also be set. Because profit is only a net figure, more detailed analysis is required in order to measure various dimensions of branch manager in attaining his objective .

Only those controllable factors that the branch manager is fully responsible for will be chosen as the targets.

¹² Net profit is equal to net interest income plus net commission income, plus other net revenue, less administrative expenses.

¹³ Controllable costs are those costs which are fully controllable by the branch manager's discretion. Examples are personnel costs and interest expenses.

¹⁴ Uncontrollable costs are those costs which are not incurred at the branch manager's own discretion. Examples are Head Office expenses and rental expense.

Based on our research study, most branch managers reflect that the following targets can be monitored by them to a great extent. For reader who have interest to know more above the reason why these targets are chosen, please refer to Appendix 7 for details relating to the branch current operation structure.

i. Average Deposit Size

The deposit level which the branch manager should be achieved throughout the budgetary period is an important target. However, to avoid manipulation of year end figure, an average balance (calculated by accumulating daily balances and then divided it by the total number of days accumulated) should be used.

ii. Quality of Deposit

The branch manager should also keep an eye on the quality of deposit in parallel with the size of deposit. The quality of deposit is measured by its stability and cost. Thus, the cheaper¹⁵ and

¹⁵ In Hong Kong, the cheapest deposit is the current account deposit, and then followed by the deposits with interest rates regulated by the Hong Kong Association of Banks.

the longer maturity of deposit the bank had, the greater the increase in profit margin of the Bank.

Hence, two dimensions, the average cost of deposit¹⁶ (on yearly basis) and the average maturity of deposit¹⁷ (on original maturity basis), on this factor are measured.

iii. Average Loan Size

The loan level which the branch manager should achieve throughout the budgetary period is another target. Similar to average deposit size, the average balance measurement should be used.

¹⁶ The average cost of deposit is calculated as follows :

$$\frac{\text{The annual interest payment (including accrual interest payment)}}{\text{The average deposit balance}}$$

¹⁷ The average maturity is calculated as follows:

$$\frac{\sum \text{Average Deposit} \times \text{Original Maturity}}{\text{Average Deposit Balance of all Kinds of Maturity}}$$

For those deposits without fixed maturity, the bank can estimate the average maturity by some statistical methods or by experience. For example, the current account deposit can be estimated as deposit with two days maturity; the savings deposit can be estimated as deposit with 14 days maturity.

iv. Quality of Loan

To avoid branch manager from expanding the loan size for the sole purpose of attaining the target and without considering the risk exposure of the loan portfolio, and consequently leading to high bad debt rate, it is important to measure the quality of loan.

There are two dimensions to measure the quality of loan. Firstly, the risk asset ratio is used. This ratio is defined as the risk assets balance divided by the total assets balance. The risk assets are defined as the interest income generating assets (usually they are loan items in the branch context) weighted by the risk factor¹⁸.

For assets with no risk or relatively lower risk, the risk factor will be equal to zero or 0.2. Examples include the loan being fully secured by the Bank's deposit certificate or being guaranteed by the Hong Kong Government.

¹⁸ This approach would be very similar to the calculation of capital adequacy ratio which is the statutory requirement by the Hong Kong Banking Commissioner (Detail of risk assets categories suggested by the Hong Kong Banking Commissioner is shown in Appendix 8).

Assets with moderate risk will be weighted by the risk factor of 0.5. Example includes the housing mortgage loan.

Assets with higher risk will be weighted by the risk factor of 1. Examples include personal loan, unsecured overdraft.

Thus, the risk assets balance may range from zero to the full asset value; and the risk asset ratio will vary from zero to one. The higher the ratio, the higher the risk profile is.

Secondly, some specific products targets for the branch manager to attain are set . The product being chosen should be in accordance with the Bank's overall strategies. For example, if the Bank wants to promote the housing mortgage, then this product will be set as a target for the branch to attain. The target is measured by the total transaction amount generated from that specific product for a specified period of time.

It is interesting to note that no average yield of loan has been measured in this context. The reason is that such target may foster the branch

manager to seek risky loan which is priced at relatively higher interest rate.

v. Commission Based Business

Beyond interest income, commission income is another major source of income for the branch but without any risk adheres to it. The current trend of banking business has gradually shifted to the commission based businesses¹⁹. Therefore, it is worthwhile to choose this source of income as one of the targets.

In the branch context, the common commission based businesses include the opening of documentary credit , remittance, insurance and loans etc.

The target is measured by the total transactions volume incurred at a specified period of time.

¹⁹ Eva To, "Banking : Adequacy Rule Approved." South China Morning Post, 28 October 1988.

vi. Operating Efficiency

Operating efficiency is defined as the efficient use of the resources in order to obtain the optimal profit. It is very difficult to measure the operating efficiency by an absolute figure measurement. Therefore, some efficiency ratios should be used as the targets.

Some common efficiency ratios are as follows:-

- a.
$$\frac{\text{Gross Profit}}{\text{Controllable Administrative Expenses}}$$
- b.
$$\frac{\text{Profit before bad debt, rental payment, tax}}{\text{Number of operating staff}}$$
- c. Interest Spread (Net of Bad Debt)²⁰

These ratios are not exhaustive. Banks can add more ratios to this factor if they think necessarily.

²⁰ Interest spread is defined as the average yield of loan (the loan balances do not include the problem loans balance) minus the average yield of deposits.

How to Measure the Branch Performance

The basic framework to measure the branch performance is to compare the extent of actual figure out-perform the standard target. Based on this concept, an achievement ratio is designed to measure each factor mentioned.

The achievement ratio is defined as follows:

$$\frac{\text{Actual figure}}{\text{Target/Budgeted figure}} \times 100\%$$

By means of Conventional Rating Scale Form, each factor's achievement ratio will be fitted into the rating scale in order to reflect its performance standard. For examples, the ratio ranged from 110% to 90% may be classified as average performance and from 130% to 111% as good performance etc. Then a numerical scale will be substituted into the performance scale.

Since not all factors have equal importance and controllability to the branch manager, different weights will be assigned to each factor to reflect for these variations. The calculation of weighted score of each factor is the result of the multiplication of the numerical scale and the weights.

The branch performance is the average of the grand total of the weighted score.

As a large number of factors is required in the branch performance measurement, we suggest the use of a separate form (may be termed as Branch Performance Appraisal Form) to do the job. The detail of the form is shown in Exhibit 6. Then the final score in the form will be input into the original appraisal form.

The Advantage of the New Appraisal System

The new system has several advantages which are not found in the current system.

1. The performance factor can be well defined in all dimensions and measured quantitatively. Ambiguity and personal bias shall be eliminated to a great extent.
2. Since the objective and targets can be well defined, the manager can negotiate with his boss in order to arrive at the agreement of his expected standards.
3. Most appraisal factors can be measured quantitatively or appraised by several raters. Most of the errors such as unreal consistency and central tendency (refer to Chapter I) shall be reduced to a minimum.

Score Items	Excellent	Good		Average		Satisfactory		Poor	Reference	Weight	Weighted score
	8	7	6	5	4	3	2	1			
Achievement Ratio	130% or above	130% to 121%	120% to 111%	110% to 101%	100% to 91%	90% to 81%	80% to 71%	70% or below			
Objective Profit									Actual _____ = _____ Standard		
Average Deposit									Actual _____ = _____ Standard		
Average Cost									Actual _____ = _____ Standard		
Average Maturity									Actual _____ = _____ Standard		
Average Loan									Actual _____ = _____ Standard		
Risk Assets Ratio									Standard _____ = _____ Actual		
Target Product									Actual _____ = _____ Standard		
Commission-based Business									Actual _____ = _____ Standard		
Gross Profit Admin. Expense									Actual _____ = _____ Standard		
Profit No. of staff									Actual _____ = _____ Standard		
Interest Spread									Actual _____ = _____ Standard		
Grand Total											
Average									Grand Total 11		

Exhibit 6. Branch Performance Appraisal Form

4. The heavy reliance on the immediate boss to perform the appraisal in the current system has been reduced because more objective measurements are introduced. Since there are more supporting evident, the boss can discuss more frankly with the manager about his performance without the fear of spoiling the relationship between both parties.
5. The new system is no more secret appraisal system (compared with the current system in which only the Personnel Department and the Department head can directly know the result). It is an open system in which everyone involved can know the result. Thus, it encourages communication and feedback which aligns with modern management philosophy.
6. Since the manager can have a solid reward for his performance, he may perceive a strong correlation with his performance and the reward system, if the reward scheme is based on this performance standard. Hence, the appraisal system can induce staff to better performance.
7. More objective data is provided to improve the current performance of the manager and to identify his strengths and weaknesses.

8. The Personnel Department can obtain more supportive evident for future staff planning and promotion.

The Problems in Implementing the New System

For the system to operate effectively, the following key issue should be solved beforehand. Otherwise, the system will be too complex to operate and the benefit obtained cannot counteract the cost incurred.

1. The BOC Group should establish a sophisticated MIS to provide the necessary data for assessing the branch performance. A fully integrated MIS is highly recommended.
2. The BOC Group should provide a budgetary system to facilitate the setting of the objective and targets, to perform ongoing review of work progress and to revise the objective and targets whenever it is necessary.
3. The BOC Group should provide a sophisticated management accounting system to assess the profit and loss for branches, departments, customers groups, product group etc. To have a true and fair profit and loss figure, many factors have to be clearly

distinguished such as fixed and variable costs, apportionment and allocated costs, controllable and uncontrollable costs, direct and transferred revenue, etc.

These three factors would be critical to the success of the system implementation, and therefore in the next chapter, a thorough study on BOC Group relating to these aspects will be discussed.

CHAPTER IV

CURRENT BRANCH PERFORMANCE

MEASUREMENT METHOD

The major quantifiable factor of the appraisal system proposed in the last chapter is performance of branch. An objective measure of branch performance is therefore critical to the new system. However, sophisticated management information, budgetary information, and management accounting information are necessary for an objective measure of branch performance.

In this chapter, we shall find out information on branch performance that is available in the computer systems. We will then study the current branch performance measurement method in order to determine whether the method is suitable for the proposed appraisal system.

Availability of Management Information
in the Computer Systems

Since the Group employs decentralized accounting system, all branches keep their own accounting records. Thus, the financial accounting data including balances of loans, deposits, revenue, and expenses are available. However, all financial data are kept on book basis by different application software separately. Average yield, average costs, and average maturity of loans and deposits of different types are also computed by the computer systems from the available data. In order to help banks to manage their risks, reports providing the most basic information such as the analysis of overdue loan are generated. Besides, there are also profit sharing reports provided by the latest systems, like foreign exchange system and bills system, but such information is not available from the systems which were developed long time ago, like loans and deposits systems.

To help banks to fulfill the statutory reporting requirements, data according to these requirements such as the classification of assets into different risk asset categories are provided to the head office of each member bank.

The Customer Information Facility (CIF)²¹ consolidates the credit exposure of bank to individual customer. Thus, banks can have a thorough understanding and a more complete picture of the creditability of customers. This is strengthened by the information on types of customer, types of security, and the usage of loan by customers. The total exposure of bank can therefore also be classified according to the types of customer, types of security and usages of loans. Such information helps banks to direct the funds to their target distribution. Finally, all the existing systems provide yearly transaction volume which allow banks to measure the work volume that a branch handles in a year.

Management Information Not Available
in the Current Systems

It seems that the current systems provide quite a lot of management information. However, there are still some important information not given by the systems. Firstly, as the Group has no complete budgetary control system and they only set targets on some board areas such as balances of loans and deposits, all systems are not designed to provide budgeted data on neither profit and loss items nor

²¹ Customer Information Facility (CIF) is a system developed by the EDP Center of BOC Group. This system consolidates information from different systems of customers with credit line. With this system, bank officers can have a whole picture of the exposure of bank on individual customer and the interest income earned from the customer.

on assets and liabilities items. Thus, the employment of budgetary control is more difficult.

Secondly, as mentioned above, the data are kept by different applications separately. The whole system cannot provide integrated data except the CIF. Thus, banks need to manually consolidate information which is necessary for management to make decision, like the overall yield of deposits and loans. However, the manual processes take a long time and need much effort to ensure the accuracy of the results.

Thirdly, most of the systems are out-dated. When the systems were designed, the branch performance evaluation concept had not been well-developed. Therefore all data were recorded on book basis. With such system design, revenue cannot be split on departmental basis and no inter-book transfer functions on the financial data are available. Expectantly, functions on the even more advanced concept and function such as transfer pricing, linking the current system to external market data suppliers' system are missed.

Without such information, banks are quite difficult to carry out a more objective evaluation on branch performance.

Description of Current Branch Performance

Evaluation Method

The Group is using the adjusted branch profit as a measure of branch performance. Branch book profit is adjusted manually by allocated revenue and expenses, transfer price, provision for bad debt, and rental value of branch premises. A branch profit and loss statement is shown in Exhibit 7.

We note that the following issues on the current branch performance measurement method need to be considered.

1. Transfer Pricing²²

There are actually no accurate transfer price established in the Group. The so called 'transfer price' on the funds attracted or used by branches are based on the average interest rate of deposit plus a pre-agreed loading.

²² According to Charles T. Horngren, transfer price is defined as charges between profit centers to which both revenue and expenses are assigned. In case of bank, the internal transfer of funding should bear the cost which is termed as transfer price.

Branch Profit and Loss Statement
For the year ended _____

Branch :

HK\$

Branch Profit & Loss as per AIM²³ Ledger

Add : 1. Allocated Revenue
 a. Bills Center
 b. Agency Business
 2. Transfer Price on Funding
 Supplied (Net)

Less: 1. Allocated Expenses
 a. Head Office Allocated
 Expenses
 b. Others
 2. Transfer Price on Funding
 Used (Net)
 3. Provision for Bad Debts
 4. Rental Value

Profits before Tax

Less: Taxation

Profits after Tax

Note

1. Bills center allocated revenue includes 50% of commission, 15% of interest revenue and 80% of foreign exchange income of revenue booked in the centers.
2. Head Office Expenses include the expenses of all cost centers in the Head Office which are allocated based on the number of employees.
3. Provision for bad debt is equal to 0.5% of the year-end loan balances.
4. For branch occupying owned property, the rental value equals to ratable value.

Exhibit 7. Branch Profit and Loss Statement.

²³ AIM, the Accounting Information and Management System, is the general ledger system of BOC Group. It can also handle departmental accounting by allocating expenses to the departments which issued the expense vouchers.

The branch deposit income is computed as follows:

Branch deposit transfer credit

= (Average balances of deposit - average balances of loans) x 'Transfer Price'

However, if average loans balance of the branch is greater than its average deposits balance, the result becomes the branch borrowing transfer charge.

2. Cost Allocation Basis

There are some back office departments in the Head Office which provide services to other departments and branches. They include the Administration Division, the Financial Management and Control Division, the Branch Administration Department, the Retail Banking Planning Department, etc. The costs they incurred, named as Head Office Expenses, should be allocated to branches in order to reflect the resources and services provided by the Head Office. Since different departments have different characteristics and require different services, the costs should be allocated on different bases. However, due to the lack of information, only simple but inappropriate methods such as number of staff in branches are employed. Similarly, revenue is also based on some pre-determined sharing ratios between branches and operating centers.

3. Specific Provision for Bad Debts

Only general provision for bad debts is assigned to branches. The provision is only 0.5% of loan balances. No specific provision for loans lent out by the branch is assigned to it.

4. Rental Value

Branches using bank's own properties are only charged for the ratable value of the properties as rent. However, for branches using leased properties, they are charged with market value.

5. Inter-books Transfer

As the computer systems have no such design, inter-books transfer is not available in the Group. All income and expenses are recognised at the place where the transaction is booked. If one wants to split the revenue and expenses according to efforts exerted by different parties, one will do many manual adjustments which is not only time consuming but also inaccurate. Thus, it discourages detailed allocation of revenue and costs.

Disadvantages of Current Branch
Performance Measurement Method

After the study of the branch performance measurement method, we find out some disadvantages.

1. Inaccurate Transfer Pricing

In the Group, some units are net suppliers of funds, such as most of the branches in the Group, while some units are net fund users such as the Treasury Departments. Funds must be therefore transferred internally from one unit to another unit. Transfer price is the costs of the unit taking up funds from other units. Thus, transfer price should be set to :

i. Facilitate the determination of interest rate of loan

For banks to have profit, interest rates of loans must be greater than the costs of funds and the costs of arranging the loan together with the returns to meet bank's requirements. Factors affecting the transfer price include the maturity, volatility, and liquidity characteristics of the loans and deposits.

ii. Enhanced profit and performance measurements

The transfer price should motivate profit center managers to improve their own reported profits while maximizing banks' total income at the same time. It should be realistic and equitable.

However, the so called 'transfer price' employed by the Group is inaccurate and inadequate because it is only on a cost plus basis which does not reflect the market condition. Moreover, no matter a branch is supplying funds or using funds, the same transfer rate is being used as the basis to compute the result of the branch. So, there is actually no basis to set the interest rate on loans and deposits other than following the market trends and this is one of the reasons why BOC Group has weak control over pricing. Besides, as the transfer price is not reflecting the market price, branch managers are not motivated to achieve their best performance and may lead to sub-optimal decision.

2. Simple Allocated System

Allocations of expenses establish accountability within the banks because the expenses are allocated to the branch which leads to the incurrence of expenses. Specific basis should be selected and it should be a function of the expenses being allocated. Moreover,

allocation bases should be developed with the thought of being fair, equitable, and relevant. The branch managers must know how the allocations are being calculated and why the bases are being chosen.

Since the allocation bases are inappropriate, the allocated expenses do not reflect the true consumption of resources by the branch. The allocation also violates the matching concept because the costs allocated do not match with the revenue generated. Furthermore, as the allocated costs are actual costs incurred by operation centers, branches may therefore bear the inefficiency of operating center.

3. Partial Set-off of Allocated Revenue

Part of revenue processed by certain operation centers are being used to set-off the expenses incurred by them. The practice demotivates branch managers to attract new businesses as not all revenue generated are taken into consideration in the measurement of branch performance. It also distorts the costs structure of the branch because not all costs are allocated to it. Thus, the analysis of revenue and costs structure of branch becomes more difficult.

4. No Specific Provision for Bad Debts

Since only general provision for bad debts is assigned to branch, the branch manager needs not to take care of specific provision. In addition, responsibility of bad debts is not clearly defined. Branch managers can escape from the responsibility of the bad debt introduced by them after being transferred to other branches or departments. It encourages the trend of lending without much emphasis on loans' quality.

5. Non-market Rental Value

Some branches use bank's own premises while others rent from third parties. Those branches rent from outsiders have to pay market rent while those using bank's own properties pay only the ratable value which is usually much lower than the market rent. Besides, branch managers cannot decide to buy or to lease the property on which they run their businesses. Thus, it is unfair to compare the branch performance on such basis.

6. Unavailability of Inter-book Transfer

Due to the limitations of the existing systems, no inter-book transfer function is available. It further discourages the detailed allocation of revenue and expenses.

All the disadvantages have clearly indicated that the existing branch performance measurement method is unsatisfactory. Branches are not measured on an equitable basis and the profitability does not reflect the true performance. Moreover, such a method does not motivate managers to do their best and may lead to sub-optimal decisions which will impair the bank's overall profits.

CHAPTER V

AMENDMENTS OF THE MANAGEMENT ACCOUNTING SYSTEM

The study on the current branch performance analysis reveals many ineffective measurements which are due to the primitive management accounting system in the BOC Group. To implement the new appraisal system, it is essential for the Group to amend its management accounting system in certain context. In this chapter, we try to look into the following four aspects which are critical to our branch performance appraisal. For easy understanding of this chapter, readers are recommended to refer to Chapter I (the organisation structure of a member bank) and the Appendix 7 when topics come across the interrelationship between branches and departments.

Transfer Pricing Analysis

In the previous chapter, the current transfer pricing method has been discussed and we discovered that such system cannot facilitate loan pricing and enhance profit

measurement and performance evaluation. Hence, purposes of transfer pricing cannot be attained.

For retail banks like that of BOC Group with huge amount of deposit absorbed from the customers through branches (one of the important targets for retail branch is to take deposit), a lot of fund transfer processes would occur between branches and funding departments such as Treasury and Merchant Banking Department. To make such departments to aware of the cost of funds, an internal transfer rate must be set up in order to facilitate the funding department to price its loans correctly and to reflect those fund-taking branches being rewarded equitably. No doubt that it is beneficial to set up an elaborate transfer pricing system which can aid the Group decisions about pricing products/services, allocating resources, and appraising performance.

Characteristics of Effective Transfer Pricing System

1. The transfer price can reflect the current market condition and should not based on the historical condition.
2. The transfer price should reflect the maturity, liquidity and volatility characteristics of the assets acquired and the deposits assumed to fund them.

3. The transfer price should reflect the true performance of the branch in the process of taking a deposit and granting a loan.
4. Responsibility for interest rate risk (the potential for changes in interest rate to impact unfavourably upon profitability due to the mismatch in repricing maturity between the funded asset and the liability assumed to fund it) should not be incorporated in the transfer price.
5. The transfer pricing system can facilitate the communication between the funding department and branches.
6. The transfer pricing system must always be updated at the time of decision so as to reflect the real cost of the decision.

The Proposed New Transfer Pricing System

According to Valerie Giardini²⁴ suggestion, the effective transfer pricing system should be based on

²⁴ Valerie Giardini, Internal Transfer Pricing of Bank Funds (U.S. Bank Administration Institute, 1983) p.29.

matched-maturity funding concept. One of the common methods which most of banks adopted is termed as Specific Matched Maturity Marginal Funds Transfer Pricing (3MFTP) System.

The concept of this system is to develop a method to transfer the branch's funds based on current market marginal funds costs with maturity (refers to repricing schedule instead of time maturity schedule) matching with that deposit taking.

Under such a system, it assumes that all the funds taken by the branch should be immediately transferred to the Treasury Department which acts as the funding center in the Bank. The funding center should 'buy' all the liabilities at appropriate transfer prices at the time the deposit transaction accomplished. The basis of setting the prices should be according to the characteristics of that deposit (such as currency, maturity, volatility etc.) so that perfectly matching is feasible. By assumption, the spot inter-bank market rate which can match the characteristics of that deposit should be used.

Since the basic deposit rate is set by the Treasury Department, which is based on the market rate with the same maturity and volatility minus a spread, if the branch manager quotes the basic deposit rate to the customer, then

the transfer price (i.e. the market rate) must be greater than the actual cost, the branch should gain a positive spread on this transaction. As the liability is 'booked' at the funding center, the transfer price will be appended to the entire life of the liability till the repricing date arrives. Thus, the interest spread will be 'locked' and not be affected by interest rate risk.

Such a process will be repeated for each deposit-taking transaction on daily basis. The funding center will 'buy' all these liabilities at various market rates which form a pool of fund to supply the funding center to place on the inter-bank market. The effective cost of the pool represents the opportunity cost for the funding center not to obtain their source of funds from the open market.

The following example may give an illustration on the 3MFTP concept.

Branch A received 3-month deposit priced at 8%.

The current market rate for lending 3-month deposit priced at 9%.

The current market rate for borrowing 3-month deposit priced at 9.25%.

The 3MFTP concept assumes the funding center will 'buy' the funds from the branch A at 9% (the best lending rate that the branch A can place at the market) and 'sell' the funds the market at 9.25% (the equilibrium borrowing rate that the borrower in the market likely to borrow).

Thus, the overall transaction can be broken down as follows:

	<u>Branch A</u>	<u>Funding Center</u>	<u>Bank Total</u>
Income	9.00%	9.25%	9.25%
Cost	<u>8.00%</u>	<u>9.00%</u>	<u>8.00%</u>
Spread	1.00%	0.25%	1.25%

Branch A has the secured spread of 1% which is a share of total profit in this transaction.

However, in real practice, the funding center needs not match its liability by a 3-month asset. It can perform the mismatching strategy by hedging with a shorter-term or longer term assets according to the expected interest rate trend. This strategy is usually determined by the Asset / Liabilities Management Committee (ALMCO) to take the interest rate risk aiming at higher profit motive. But the result of this decision will not affect the Branch A's transfer profit. Since the details of this mismatching concept is out of our study scope, we will not go on further discussion.

In the case of branch having loan transaction, it has to borrow fund from the funding center. There is no netting of deposit and loan within the same branch because the maturity to the deposit and loan may not be perfectly matched. Therefore, under the assumption of '3MFTP' branch should have all assets and liabilities matched perfectly and no self-netting is allowed. Moreover, this requirement facilitates the budgetary plan for branches because branch managers can be easier to estimate the cost of loan financing and the yield on the deposit-taking.

Further to our previous example, the funds-taking by the branch A is being used by the housing mortgage priced at 12%:

The overall transaction is amended as follows:

	<u>Branch A</u>		<u>Funding Center</u>	<u>Bank Total</u>
	<u>Loan</u>	<u>Deposit</u>		
Income	12.00%	9.00%	9.25%	12.00%
Cost	<u>9.25%</u>	<u>8.00%</u>	<u>9.00%</u>	<u>8.00%</u>
Spread	2.75%	1.00%	0.25%	4.00%
Total spread	3.75%			

Advantages of the New Transfer Pricing System

1. The system can reflect the most realistic transfer price which the branch should entitle. Thus, it helps to improve the branch performance measurement.
2. A secured spread for each deposit-taking transaction.
3. The branch manager may be motivated to attract lower cost deposits in order to enlarge the spread of the transaction. On the other hand, the manager may be demotivated to attract higher cost deposit or grant privileged interest rate (i.e. offering a higher interest rate than that of basic rate) so as to attract more deposit. Thus, the system helps the Group to control the cost of deposit.
4. The branch manager need not assume the responsibility of interest rate risk which is shifted to the funding center under the guidance of ALMCO.
5. A three-way analysis of interest spread (i.e. pricing, funding, and mismatch) becomes possible.
6. Two-way communication is provided between the funding center and branches because of deposit-taking branches will notify the fund characteristics of each

transaction to the funding center so that it can have first hand information to facilitate its mismatching strategies.

7. The spread generated by the funds-taking and the spread from loan granting can be separated. Thus, the relative efficiency and profitability can be measured and evaluated.

Problems Encountered by the System

1. The system requires an elaborated software package to perform all functions such as data capturing, spread calculations, average yield calculation, revenue allocation, data control, back up procedures etc. Especially for BOC Group, each branch may have a several thousand deposit transactions which may lead the system to grow very complex.
2. A specialised department has to be set up to handle the transfer pricing system, monitor its operations and receive feedbacks from branches.
3. It is difficult to capture the market price of each deposit transaction occurred at different point of time. Unless the mainframe can provide such data,

some daily generalized market price may be employed to each day's transaction. Thus, the accuracy of the system may be affected.

4. The branch manager may feel difficult to interpret the system.

Cost and Revenue Allocation Systems Analysis

In the previous chapter, we have discussed that the current allocation system in the BOC Group is not well developed. Some arbitrary allocation bases are used which may not be relevant to the function of the expense incurred. Moreover, there are not many inter-book transfers of revenue between two profit centers so that revenue may be overstated or understated in some cases when a profit center performance is measured. Therefore, a comprehensive allocation system with equitable, consistent, logical, and conceptually explainable framework is a necessity for measuring the true performance of a branch.

There are three types of allocation processes within banking organisation. They are the allocations for funding, revenue and expenses. Funding allocations are used in interest credit or a charge for funding transfer. The details of this part have been discussed in the previous section - Funding Costs Analysis. Revenue

allocations are used to give revenue to different units when there are two or more units participating together in the production of the same revenue stream, but the accounting profit is not booked in all of them. Expense allocations are demanding tasks especially in those complex organisation structure involving many inter-related cost centers, staff units, line units etc. This requires a lot of equitable determination in allocating the expenses to the appropriate users.

Revenue Allocation System

1. Characteristics of an effective Revenue Allocation System

This system is relatively simpler than that of funding allocations and expense allocations. The main theme is to identify the sources of income arising from. They can be the result generated from the product or customer. If the product or customer related to two or more profit centers, there should be a sharing revenue for their part of contribution in performing the service.

The criteria in revenue allocation in a banking organisation are as follows:

- i. If the customer or product generated revenue involving credit risk, then the total interest based revenue should be allocated to the ultimate profit center which bears the credit risk.
- ii. The commission based revenue (e.g. the commission from opening documentary credit) should be allocated to profit centers according to their proportion in contributing the efforts, or the nature of commission whether it can directly relate to the effort put.
- iii. The revenue generated related to the funding aspect (e.g. the exchange profit arising from the buy and sell of foreign currency from the customer) should be allocated to the ultimate center which provides the funding.
- iv. When a customer or product is introduced by other profit center to the service-providing center, the latter one should receive the total revenue generated from the customer or product and the former one should receive the referring credit. The amount of credit is subject to negotiation.

- v. When one profit center books loans on behalf of another center, the booking center should receive a share of commission to compensate its services.

2. The application in the BOC Group

According to the criteria, some of the revenue in the BOC Group should be allocated following the rules.

- i. The branch should not share any revenue with the Bills Center (including interest income, commission income, exchange profit) because the credit risk and funding costs are all born by the branch, and the total income generated from the customer should be reflected on the book of the branch. (N.B. The current practise is that the total revenues generated from documentary credit are booked in Bills Center) The Bills Center operation costs in fact should be allocated to the branch which will be discussed in the next chapter.
- ii. The Merchant Banking Department should give the referring credit to the branch which introduced the customer to the Department because the special needs from the customer cannot be catered by the branch. (N.B. Since the customer

had been shifted to the Merchant Banking Department, all the revenue generated was booked in the Department.)

- iii. Branches should be entitled the commission fees of agency business such as credit card business and insurance business.

Expense Allocation System

1. Characteristics of an effective Expense Allocation System

Expense allocation is one of the complex issues in cost analysis within an organisation. The primary aim is to allocate expenses incurred in the cost center equitably for the purpose of measuring profitability.

To set up an allocation system, the first job is to identify the costs center and profit center. This may involve detailed study of the department's function before the conclusion can be drawn. Moreover, the operation center (i.e. the department provides piecemeal services to the profit center) may need special treatment in this system. Therefore, such an identification should be based on the objective of the allocation system : what kind and how much of the

expenses should be remained in centers after the transfers out and transfers in have occurred.

Based on the system objective, the orgainsation should determine the flow of the cost absorption. Identifying and tracking the flow of costs from one center to another center would be a challenge task because a lot of research on the center's inputs and outputs relating to a particular activity should be done. It may be helpful to prepare flowcharts to track cost flows. There are several variations depending on how complex the system is.

- i. Cost centers to profit centers only
- ii. Cost centers to cost and profit centers
- iii. Cost centers to cost centers and then to profit centers
- iv. Cost and profit centers to profit centers

Combination of these variations are possible. However, the more combinations of variations, the more complex of the system is. Management should justify the cost and benefit according to the system objective. Once the cost flow direction is determined, the sequence of the cost flow among cost centers can be determined.

Based on the nature of services provided by cost centers to profit centers / cost centers and the ways that services consumed, the organisation should formulate the allocation base for different cost centers or services. The criteria of choosing the bases must be relevant (to certain extent) and representative but should not be too costly to determine and to administer. Some common bases found in banks²⁵ are as follows:

- i. Number of staff in each center
- ii. Number of branches
- iii. Average deposit balance
- iv. Average loan balance
- v. Number of vouchers
- vi. Number of transactions in counts
- vii. Space occupied
- viii. Number of computer terminals
- ix. Number of accounts
- x. Interest income / expense
- xi. Arbitrary weighting

²⁵ Leonard P. Cole, Cost Analysis and Control in Banks (Boston, Bankers Publishing Company, 1985). pp.160-161.

However, to choose a suitable base for allocation may be a difficult task because different centers have different perception relating to the rate of absorption. For example, one branch may accept the computer cost in the Computer Center to be shared by the number of computer terminals but another branch may regard the number of accounts to be more reasonable. Therefore, the cost analyst should develop the allocation bases with the aim of being fair, equitable, and relevant.

Finally, the organisation should choose the methods of allocation of expenses. There are essentially two methods: sequential and simultaneous closeout.

Under the sequential method the expenses are closed out from one center to another. Once the cost center allocates its expenses, there is no reallocation back to it. The simultaneous process involves multiple allocations between centers concurrently. A center receives allocation from other centers that is also a recipient of the former center allocation. This method can be complex in execution.

The application of which method should rely on the management's philosophy.

2. The application in the BOC Group

Data capturing in the BOC Group in the center can be fully handled by the Accounting Information and Management System(AIM)²⁶. There is no problem in gathering the necessary expenses data. The function of each department and its relationship with branches are all well defined (Refer to Chapter I and Appendix 7). The major steps to be further elaborated are the determination of the cost flow sequence and the allocation bases.

Our proposed cost flow sequence is shown in Exhibit 8.

The first level expense allocation are started from the basic cost centers which incur the general overheads to the Group. Examples are Personnel Department, General Affairs Department etc. Their costs will be allocated to all other cost centers and profit centers. The second level of allocations are started from the indirect supporting cost centers which do not have direct relationship with the branch's performance. Examples are Accounting Department, System and Method Department, etc. Their costs include direct costs and allocated costs from

²⁶ Functions of AIM are explained in Exhibit 7.

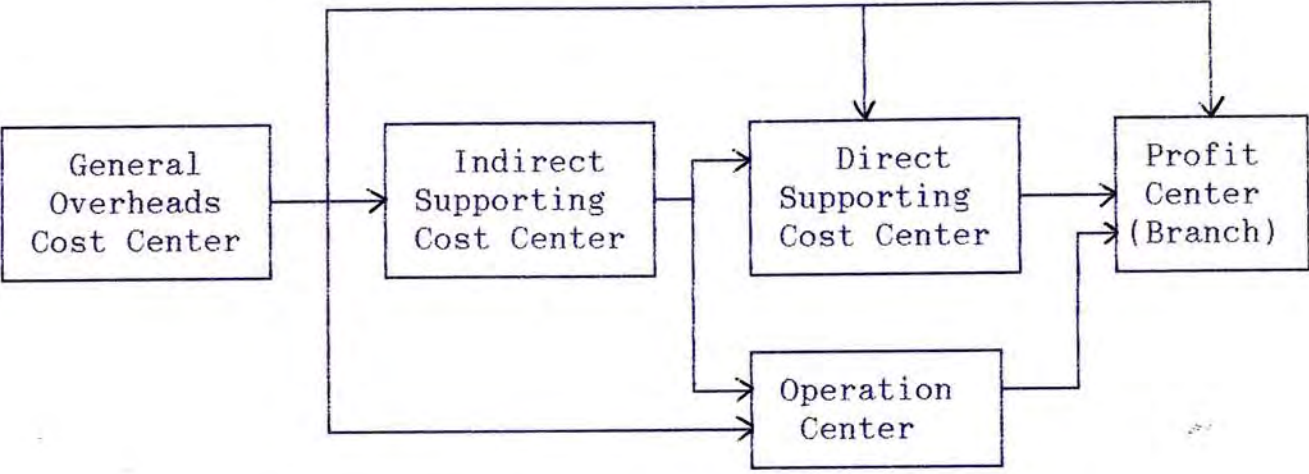


Exhibit 8. The Cost Flow Sequence in BOC Group.

first level cost centers. Similarly, their costs will be allocated to final level cost centers and operation centers but will not be allocated directly to profit centers. The final level of allocations are started from the direct supporting cost center and operation center. They all have direct relationship with the branch's performance. Examples are Branch Administration Department, Retail Banking Planning Department, Bills Center and Loans Department.

The determination of the cost flow sequence can help the Group to select the cost allocation bases equitably and relevantly. For example, the allocation of general overhead of cost centers may be based on a more broadly defined base such as number of staff. The allocation of costs of indirect supporting cost center may be based on a more specific base such as the number of vouchers or number of jobs performed. Finally, the direct supporting cost center can break down its cost into small units according to the functions provided. Then the branch will absorb the cost according to the services it has used. For example, the Branch Administration Department has provided services for the administration of loans portfolio. The cost of this part (including direct and allocated costs from other cost centers) may be allocated at the average loan balance basis while the

other part of costs may use other bases if appropriate. The operation center may use piecemeal basis because of its special nature. The detail of the cost allocation on this special center will be discussed in the next section.

It is true that not all costs should be allocated. For example, shared costs arising from the Hong Kong and Macau Regional Office are not related to any center's performance, and no one can account for this cost. To avoid distortion of the cost structure, it would be better not to take any action.

Advantages of the Allocation Systems

1. The system provides meaningful way to measure the branch profitability.
2. The system fosters the development of departmental accounting and product costing.
3. The system entitles the branch to differentiate the controllable and uncontrollable expenses (i.e. direct and indirect expenses) which will help the branch to

budget the profit objective and explain the responsibility whenever variance arises.

4. Branch managers will be motivated to achieve the objective and targets because they can enjoy all the revenue due to their contributions and assume the cost they should bear. In short, the manager's performance can be measured equitably.

Problems Encountered by the System

1. The more detailed the allocation system, the more allocation bases are required. But it is not easy to obtain all necessary allocation bases because some data may not be completely obtainable from current computer systems.
2. It is very time consuming to negotiate with all centers to gain overall consensus and understanding of how allocations are being calculated before they can accept the system.
3. The more complex the system, the more inflexible the system becomes. However, such a system should be adapted to changes that often arise from growth of business, change of organisation structure and shift of management philosophy.

4. A specialised department should be set up to convey the information, manage the system, and adapt the changes upon requests.

Standard Costs Applications

Chapter I has discussed the current organisation structure and introduced a special type of cost center - operation center. It is a technical support center which provides specialised and professional services to the profit center so as to improve the efficiency and quality of services to customers. Two typical examples can be found in BOC Group - the Bills Center and Loans Department. The functions of the former one are providing the operation procedures relating to documentary credits (e.g. opening and checking Letter of Credit) and the latter one are providing the processing and checking of loans documents.

The major difference between a cost center and an operating center is their relationships with the profit centers. A usual cost center does not have direct relationship with the profit center. It provides general services to the whole organisation. Thus, its cost will be apportioned on some general basis. Even though some special cost centers(i.e. direct supporting cost center) may have more clearly defined relationship with branches,

the services they provide are general in nature and is not specific to a particular branch. On the other hand, the operation center provides services solely to branches which request for such services. Since the service is on job basis, the operation center can define a very unique relationship with a particular branch quantitatively by means of transaction volume measurement. Due to this special characteristic, the operation center should charge its costs to branches on unit cost basis instead of some general apportionment methods.

The current methods of handling the cost of such operation centers are not appropriate. The Bills Center does not allocate its cost to branches which may understate the operating cost of branches. The Loan Department using the general apportionment basis does not reflect the true relationship with branches.

In fact, the employment of unit costing method may be suitable in this case. The unit costing method would be based on actual historical costs incurred divided by actual volume of activities. However, using this method the branch cannot pre-estimate its operating cost concerning the operation center because there is only historical figures, and the inefficiency of the operation center may be transferred to the branch since the unit cost is on actual basis.

Development of Standard Costing

To avoid the loopholes of actual unit costs, we proposed the Group to use the standard costing method. Since the standard unit cost derives from budgeted / standard figures, it can be predetermined at the beginning of the financial year and hence facilitate budgetary planning.

In using standard costing, it is important the activity in the operation center can be standardised, and the sequence of tasks leading to the completion of an activity can be tracking out. By using the work measurement techniques to check for the time base against each task, an activity-aligned standard time is developed. Such a standard time factor will be the base to calculate the standard labour cost and standard operating cost provided that the standard labour rate and standard operating cost rate have been known. Thus, the standard unit cost per activity is the sum total of standard labour cost and standard operating cost. If there are more than one activity in the operation center, each of them will be analysed and the aforesaid procedures will be repeated to find out the standard unit cost.

Based on this standard unit cost, the branch manager needs to estimate the volume of transactions (in units) only and the total costs can readily be estimated by multiplying these two factors. Moreover, the transaction volume is under the control of the branch manager. He should be the person responsible for the explaining of the actual and budget cost difference because the variance is solely due to the volume variance (i.e. there is no price variance because the standard unit cost rate does not change).

Advantages of the Standard Costing

1. Branch managers can control the operation centers' expenses more efficiently because they have to control the volume variances only and do not need to take care of spending variances and efficiency variances in the operation center.
2. Operation center managers can be measured by the effectiveness on the control of spending variances because they do not need to take care of the volume variance. Moreover, the time standard set up for each activity helps managers to sort out unfavorable efficiency variances which may be meaningful for management to decide on human resources planning and work procedures design in the operation center.

3. Standard costs allow branch managers to have a more stable planning of costs and make prediction more reliable.

Problems Encountered by the System

1. The employment of standard costing system²⁷ is very controversial because the concept may be difficult for people to understand and they may prefer actual cost figures as data are self-explanatory. Some people regard the standard cost system is too elaborate and feeds them too much data more than they can assimilate. Therefore, employees may need education before the system can be implemented.
2. Sometimes, the actual costs and standard costs may have great difference. If the branch prices the product / services based on the standard cost, the overall profit margin may be reduced in case of unfavorable variance. Unless the Group can reconcile the actual and standard costs frequently, sub-optimal decision may exist.

²⁷ Leonard P. Cole, Cost Analysis and Control in Banks (Boston, Bankers Publishing Company, 1985). p.119.

3. It is expensive to maintain the system because it requires cost analysts, organisation and method analyst, and programmers to cooperate. Moreover, on-going review procedures have to be implemented in order to update the standard as soon as possible.

Budget Planning Process

The most powerful control should be direct supervision because you can redirect the activity at once while you discover deviation. However, in the business world, the management is attempt to control a lot of complex operations of great diversity so that it is infeasible for the management to execute direct supervision. To assist the management to execute the control, accounting controls thus form a vital part of the control mechanism. One of the accounting control techniques is budgeting. It enables a standard of performance to be set up which will be used to measure against the actual performance.

There are two main aspects of budgetary control. First, it is a systematic way of planning in terms of the many constraints on organisation activity. Second, it is a management control device designed to ensure the agreed objective and targets can be achieved according to the company's policies.

Multiple Roles of Budgeting

1. Authorisation

The formal document to approve the responsibility of the manager with respect to his resource utilisation and return on such a utilisation.

2. Forecasting and Planning

Budget attempts to control the future based on the current controllable events.

3. Communication

Budget can help managers in different centers to coordinate their activities by frequent interaction during the budget setting process.

4. Motivation

Budgets may be used to motivate managers to achieve organisational objectives. Thus, it is important to allow managers to participate in setting their standards or to understand how to establish their standards so that they can regard the budget as their personal goals for achievement.

5. Performance Evaluation

Budget is the one of the effective quantitative measures of managers' performance by comparing the actual with standard performance.

Applications in BOC Group

Since there is no elaborate budgetary system in the BOC Group, only some targets forecast such as deposit balances, loan balances, commission-based business volume, etc. are made by the corporate management. The process will be ended when such forecast have been communicated to branch managers.

However, if the new appraisal system requires a new performance evaluation method, a more elaborate budgetary system should be developed in order to help manager to set up targets and standards. How to set up the standards and targets are the most controversial issue because the level of the performance would be affected by such standards and targets. If there is no way to set up objective standards and targets, the performance evaluation may be unreliable. To overcome the difficulty, the concept of Management By Objective (MBO)²⁸ should be applied in this case.

²⁸ Management By Objective is a mean for translating key corporate strategies into operational objectives and plan.

1. Set up of MBO committee

A MBO committee is set up to aid the managers to formulate their performance standards. The committee consists of the head of the Retail Banking Division, the head of Branch Administration Department, the head of Retail Banking Planning Department, the branch managers and the head of Financial Management and Control Division.

The head of the Retail Banking Division will provide the overall objective and direction of the bank in the branch banking business. The head of the Retail Banking Planning Department and the head of the Branch Administration Department will formulate the strategies for each branch. The Financial Management and Control Division will provide the update management accounting information such as standard unit cost. Then the branch manager will derive his own objective and targets according to the strategies set on him in order to attain the overall bank's objective. The head of the Financial Management and Control Division will justify the branch's objective and targets are reasonable or not by comparing with other branches' projections and its own historical performance data.

The members in the committee will freely exchange their opinions in order to compromise a final acceptable objective and targets for each branch. Moreover, the branch manager can challenge the funding transfer price calculation, the allocation bases, and the standard unit costs if he feels that such factors are not fair and equitable toward his performance evaluation. The head of the Financial Management and Control Division should be responsible for handling these questions and take thorough study to check any amendment necessarily. Discussion will be continued until final compromise arrives. Once the objective and targets have been agreed, the branch manager should compile the branch budget which will be later acting as the budgetary control. Thus, the branch manager should feel great participation and commitment to the standards.

2. MBO Committee Review Process

In order to make the objective and targets more realistic, a continuous reviews and update of the objective and targets may be necessary.

Thus, the committee will schedule several meeting to review the reasonableness of the budget and study the effects upon the branch performance due to the change of the economic condition and banking environment.

If there are abnormal deviation from the budget, a thorough investigation should be performed.

The committee members may then carefully distinguish the controllable and uncontrollable factors (e.g. The lost of deposit due to the branch services will be controllable but due to political unstability will be uncontrollable) so that the branch manager need to explain the causes of controllable factors. Moreover, the actual performance of the branch will be adjusted in order to exclude all the extraordinary or uncontrollable factors and thus to make the comparison with the standard more meaningful and convincing. Consequently, the achievement ratios may be reperformed under the compromise in the committee.

Advantages of the Budgetary System

1. A more objective measurement of branch managers' performance enables the top management to exercise control actions because problems can be revealed effectively.
2. Branch managers appraisal can be measured quantatively.

3. Branch managers are motivated to attain the objectives and targets because they have committed their personal goals into the objectives during the MBO process.
4. The ongoing review process enables the bank to detect problem areas just in time and take remedial actions if necessary. Branch managers can continuously review their standards and concentrate their efforts and resources upon these controllable items.
5. MBO committee enables the communication between the manager and his bosses and other function managers. This will improve the understanding within the organisation and between superiors and subordinates.

Problems Encountered by the System

1. The success of the branch budget planning will depend on the development of the management accounting system. The more elaborate the system, the more data available for the budget planning, and the more meaningful the budget is likely to be.
2. Budget planning involves forecast which is most likely based on historical data from various dimensions. Therefore, the BOC Group's MIS should provide a

comprehensive database to satisfy the requirements. Moreover, not all managers can employ sophisticated forecast techniques in preparing budget figures and this will affect the reliability of the budget.

3. MBO process may be very time consuming because it requires a lot of negotiation and discussion, especially when there is goal incongruence between various centers. Moreover, since the MBO committee involves senior management, the cost for the system to operate would be relatively higher.
4. Once budget has been set, actual performance compared with standard performance is regularly reported. The variance analysis method should be set up in order to facilitate the managers to understand the causes of variances. Otherwise, the figure itself does not constitute any meaning if the manager cannot investigate the reason thoroughly.

The Branch Profit and Loss Statement
under the New Scheme

The purpose of suggesting the improvements in the BOC Group's management accounting system is to facilitate the preparation of the Branch Profit and Loss Statement. The objectives of the statement are to compute the controllable profit/loss (i.e. the objective set in the MBO) and the final profit/loss. The former one reflects the performance of the branch manager and the latter one is to measure the survival ability of the branch.

The format of the Branch Profit and Loss Statement is shown in Exhibit 9. Readers can contrast it with the old statement shown in Exhibit 7.

The new statement has made some structural changes in the allocated revenue and allocated expenses. The booked profit and loss is adjusted with these two factors and the transfer price credit to arrive at the controllable profit/loss. Besides, the new statement includes extraordinary items in order to separate those items which are approved by the MBO committee that should not be included in the ordinary activities of the branch and the manager should not be responsible for. Moreover, the provision for bad debt is not counted as the controllable

factor because the problem loan ratio in the branch manager appraisal form has evaluated this factor. Thus, it is deducted after controllable profit/loss. Finally, the rental value which should be either at actual value or at fair market value is deducted. The final profit/loss is provided for the top management to evaluate the branch going concern capability under full absorption cost basis.

Branch Profit and Loss Statement
for the year ended

Branch Name:

	HK\$ <u>Budget</u>	HK\$ <u>Actual</u>	HK\$ <u>Variance</u>
Branch Profit & Loss as per AIM Ledger			
Add : 1. Allocated Revenue :			
a. Bills Center			
b. Loan Booking			
c. Agency Business			
d. Others			
2. Deposit Transfer Revenue			
Less : Loan Transfer Charge			
Less: Allocated Expenses			
a. Bills Center			
b. Loans Department			
c. Direct Supporting Department			
d. Others			

Controllable Profits/Loss

Add :	Extraordinary Items *1 (Net)
Less:	1. Uncontrollable Allocated Expenses *2
	2. Provision For Bad Debt *3
	3. Rental Value *4

Final Profits/Loss

Less: Taxation

Profits After Tax

Note : *1. Items approved by MBO Committee should not be accounted for by the Branch Manager.

*2. Uncontrollable allocated expenses include the allocated expenses from general overhead cost centers, indirect supporting cost centers.

*3. Provision for Bad Debt includes specific and general provisions.

*4. Rental Value based on actual rental for leased premises or based on fair market value for owned property.

Exhibit 9. The New Branch Profit and Loss Statement.

CHAPTER VI

INTEGRATION OF THE PROPOSED APPRAISAL SYSTEM

AND THE CURRENT COMPUTER SYSTEM

The proposed appraisal system requires a lot of quantitative data on the performance of both manager and the branch he managed. If all relevant data are gathered manually, the costs will be tremendously high and it will be difficult to justify the benefit envisaged. However, with the help of computer, the process is much easier and the cost involved will also be reduced. Moreover, the existing computer systems have already capture some of the essential data. Integrating the proposed appraisal system with the current computer system is the natural development.

Appraisal Factors to be Measured by Computer

Among the eight appraisal factors of the new appraisal system, three can be measured by the computer system provide that adequate changes are made. They are 'branch performance', 'business knowledge', and 'problem loan ratio'.

1. Once the transfer price, the standard costs, the allocated bases of revenue and expenses are determined, the computer systems which maintain the branch book profit can be adjusted according to the decisions. The adjusted branch profit can then be computed and recorded by computer. The adjusted profit together with the budgetary profit determine the score of 'objective profit' in the branch appraisal form. Moreover, current systems have already maintained data required to compute score of other factors, such as the average balances, interest rate and maturity of deposits, the average loan balances, the interest spread, etc. Therefore with some changes in the computer systems, the computation of the final score of the branch performance appraisal form can be automated. Thus, the score of the appraisal factor - 'branch performance' can be filled in immediately.
2. The personnel records which are maintained by personnel department in personal computers had already included branch manager's education level, experience and training courses attended. Thus, the score of 'business knowledge' can be easily obtained.

3. All loan transactions are recorded by the loans systems. By adding the function in the system to record the manager's identity, the system will be able to collect all the loans information relating to the individual manager who is responsible for granting those loans. Together with the problem loan record, the system will be able to provide the problem loan ratio of the manager and the score of that factor can then be determined.

Suggestions on the Change of Computer Systems

Although the existing computer systems keep the essential data, they do not meet the exact requirements in the proposed appraisal system. So as mentioned in the previous section, the related systems should be changed. The systems should provide consolidated data such as the average balances of all deposits instead of average balances of different types of deposits. Integration which is one of the major problem in the existing systems should be improved. Otherwise, it will hinder the automation of the BOC group. Besides, BOC Group should emphasize requirements of management information during system design of any new computer application. Information on different aspects can therefore be provided to management for their evaluation of performance of branches and branch managers.

In the ever-changing banking world, new environment and new products appear frequently. The measurement of performance should also follow the changes. Thus, the computer system should be flexible enough to cope with the changes.

Since personnel records are kept in the personal computer of the personnel department, the linkage of departmental computer with the host computer will facilitate the exchange and combination of data between them. With such linkage, automation of the appraisal process will be able to take a further step and the manual interruption is reduced to a minimum.

It will take a long time and a high cost to implement all the suggested changes. However, such changes do not just benefit the appraisal of branch managers. The most important effect is the increase in effectiveness and efficiency of the MIS. Thus BOC Group can cope with the ever-changing world and compete with banks in Hong Kong. The beneficial effect on appraisal system is only a by-product, and management should not worry about the justification of the cost of such changes for the appraisal of branch managers.

CHAPTER VII

RECOMMENDATIONS

We have a detailed study on the appraisal system and the management accounting system of BOC Group. We discover that a lot of areas need to be improved and numerous problems are waiting to be solved in implementing our proposal. In order to enhance the feasibility of our suggestions, we recommend the Group to follow the following procedures to implement our proposal if it is accepted.

1. Since there are a lot of preparation works and coordination tasks, each member bank should establish a specialised department to implement our proposal. The main responsibility of the department is to solve all the management accounting issues.
2. The specialised department shall cooperate with the personnel department to amend the branch manager's appraisal form according to our suggestions. As the measurements of some suggested appraisal factors such as those conducted by peer review will require no significant change in our existing systems, they can be implemented at the initial stage.

3. It is important to brief all managers affected by this new appraisal system including both appraisers and subordinates so that they can gain a thorough understanding of the objectives and the operations of the new system. Their understandings will probably lead to their cooperation and participation which are the determinant factors in the success of our proposed system.
4. Another critical part of this project is to improve the management accounting system and to incorporate the system into the Group's host computer in order to automate most of the routine calculations and reportings. It is important to develop the transfer pricing system first because this part affects the branch's performance evaluation most and involves complex and tedious calculations which are unlikely to be performed manually. The allocations system and standard cost system can also be developed simultaneously. A working group, comprising of staff from some of the specialised departments of member banks and representatives of the EDP Center and the Regional Office, shall be formed. The working group should be responsible for carrying out the requirements study. Having approved by the Regional Office, the requirements should be implemented by the

EDP Center.

5. In parallel with the development of the management accounting system, areas relating to the current applications such as the integration of databases to provide consolidated information and the linkage of personal computers of personnel departments and host computer can also be suggested.
6. The system development period may extend for one to two years. The specialised department should provide on-the-job training on the new management accounting system to branch managers during this transitional period. Some manual procedures to imitate the transfer price system, allocation system, and standard cost system may help branch managers to adapt the new system which will be employed in the near future.
7. Finally, when all the management accounting data are well-prepared, the budgetary system can be implemented and the MBO Committee can also be set up to facilitate the budgetary control process.

We expect that the whole implementation process requires at least two to three years for completion. Nevertheless, it is not important to consider how long such a process can be accomplished because the most effective

management accounting system should be a never ending improvement process so that it is flexible enough to adapt and adjust for the ever-changing business environment. Indeed, the most critical step is when the organisation starts the first step to improve the management accounting system and let the branch manager to perceive that his performance can be measured objectively and quantitatively through the system.

Appendix 1(a)

Structured Questionnaire for Interview with the Personnel Manager of the Hong Kong and Macau Regional Office.

1. What are the appraisal procedures?

Do they apply to all level of staff? If not, what are the differences?

2. Are they the standard procedures in appraisal for the whole BOC Group?

3. What factors are measured in the appraisal?

Are they known to the staff being appraised?

4. How long has the current method been used?

5. Is there any plan to change the current procedures?
Why?

6. Is there any suggestions to improve the current appraisal system?

Appendix 1(b)

Structured Questionnaire for Interviews with Personnel Managers and Branch Administration Managers.

1. What is your basis in evaluating your subordinates?
2. Do the results of appraisal affect the rewards and promotion of subordinate?
3. What actions do you take to ensure the objectivity of the appraisal?
4. What problems do you encounter in the appraisal process?
5. Do you tell the subordinates the results of appraisal including their performance, weaknesses and strengths?
6. Are there any complaints on the appraisal system?
7. In terms of accuracy in measuring subordinates' performance, do you think the current system is an effective one?
8. What is your comment on the current appraisal system?
9. Do you have any recommendations on improving the current system?

Appendix 2

Questionnaire

Section A

Please circle one of the numbers (1-5) to show your degree of agreement about the following statements.

1. The current appraisal system

	Agree			Disagree	
(a) Measure your performance objectively	1	2	3	4	5
(b) Motivate you to do your best	1	2	3	4	5
(c) Measure your strengths and weaknesses	1	2	3	4	5
(d) Improve communication on your performance between your boss and you	1	2	3	4	5
(e) Has effect on your promotion	1	2	3	4	5
(f) Affect your reward	1	2	3	4	5
(g) Enables your boss to know your performance	1	2	3	4	5

2. Factors being measured in the current appraisal system

(a) are known to you	1	2	3	4	5
(b) are sufficient to reflect your actual performance	1	2	3	4	5

3. The following factors should be taken into account in your appraisal.

(a) Allocated costs eg. Head office allocated expenses	1	2	3	4	5
(b) Shared revenue eg. commission shared with Head Office.	1	2	3	4	5
(c) Personnel costs eg. salaries of staff in your branch	1	2	3	4	5
(d) Business costs eg. electricity bill	1	2	3	4	5
(e) Loan size of your branch	1	2	3	4	5
(f) Deposit size of your branch	1	2	3	4	5
(g) Growth rate of loan in your branch	1	2	3	4	5
(h) Growth rate of deposit in your branch	1	2	3	4	5
(i) Budgetary control	1	2	3	4	5
(j) Branch location	1	2	3	4	5
(k) Head Office support	1	2	3	4	5

4. The current computer system can provide information

(a) to reflect the true operating costs	1	2	3	4	5
(b) to reflect the true business revenue	1	2	3	4	5
(c) to reflect your performance	1	2	3	4	5
(d) which help you to make better decision	1	2	3	4	5
(e) which allow bank to carry out responsibility accounting system	1	2	3	4	5

5. Your suggestion on the improvement of current appraisal system.

Section B

6. Your current post is
- ☐ Assistant General Manager
 - ☐ Senior Manager
 - ☐ Manager
 - ☐ Deputy Manager
 - ☐ Others. Please specify:

7. You have held your current post
- ☐ Less than 1 year
 - ☐ 1 - 5 years
 - ☐ 6 - 10 years
 - ☐ More than 10 years

8. Your working experience with BOC Group
- ☐ Less than 1 year
 - ☐ 1 - 5 years
 - ☐ 6 - 10 years
 - ☐ More than 10 years

9. Your monthly salary is
- ☐ < \$10,000
 - ☐ \$10,000 - \$15,000
 - ☐ \$15,000.01 - \$ 20,000
 - ☐ > 20,000

10. Your age is
- ☐ < 30
 - ☐ 31 - 40
 - ☐ 41 - 50
 - ☐ > 50

Appendix 3

Structured Questionnaire for Interview with Manager of Accounting Department.

1. How do you evaluate the branch performance?
2. Do the current computer systems provide the data you need?

Is there any function or feature specially designed in the systems solely for the purpose of branch performance evaluation?
3. Do you think the current method is an effective one?
4. Do branches complain about the result of assessment?

Do they concern about the result? What actions are taken to response the complaints?
5. Do you encounter any problems or difficulty in the evaluation?
6. What are your suggestions for solving the problem and for improving the current method?
7. Do you have any plan to implement your suggestions?

If no, why?

Appendix 4

Structured Questionnaire for Interview with Manager of
System & Method Department.

1. How many computer systems (application software) are on production in BOC Group?
Are they the same for all member banks?
What are their major functions?
Who are the users?
2. Are there any linkage between the systems? If any, please explain.
3. Do all the systems in-house developed by the EDP Center?
4. Is the host computer the only computer used by your bank? If no, what are the other machines? What application is handled by the non-host computer? Are there any linkage between the host and other machines?
5. Do the systems provide adequate information to users?
Do they meet the requirements of users?
6. Do users have complaints on the computer systems?
What actions are taken in response to the complaints?

7. Is there any problem in the computer systems?
What are the problems in developing new systems?
8. What are your suggestions for solving the problems and
for improving the current systems?
9. Did you try to implement you suggestions?
If no, do you have any such plan? If no, why?

Appendix 5

Summary of Results of Questionnaires

Question	Score					Mean	Standard Deviation
	5	4	3	2	1		
1(a)	4	24	11	2	1	3.667	0.8067
1(b)	4	8	22	6	2	3.143	0.9404
1(c)	19	9	12	2	0	4.071	0.9610
1(d)	15	17	8	1	0	4.048	0.9246
1(e)	0	16	12	10	2	3.119	0.9562
1(f)	0	2	17	13	10	2.261	0.8745
1(g)	13	13	16	0	0	3.929	0.8279
2(a)	4	12	10	16	0	3.095	1.0191
2(b)	15	18	5	2	2	4.000	1.0465
3(a)	34	8	0	0	0	4.810	0.3927
3(b)	28	10	4	0	0	4.571	0.6598
3(c)	16	19	4	3	0	4.143	0.8611
3(d)	0	1	7	28	6	2.071	0.6322
3(e)	1	1	6	23	11	2.000	0.8452
3(f)	0	4	11	12	15	2.095	0.9955
3(g)	0	2	13	20	9	2.214	0.8028
3(h)	2	1	8	12	19	1.929	1.0778
3(i)	17	15	8	1	1	4.095	0.9464
3(j)	12	18	7	3	2	3.833	1.0672
3(k)	5	12	15	4	6	3.143	1.1867
4(a)	10	21	8	2	1	3.881	0.9051
4(b)	1	6	27	8	0	2.952	0.6529
4(c)	8	16	12	4	2	3.571	1.0498
4(d)	14	20	6	1	1	4.071	0.8835
4(e)	18	16	5	2	1	4.143	0.9654

Appendix 6

Description of the Appraisal Factors of the Managerial Grade.

1. The 'business achievement' measures whether the manager can attain his assigned business target or not.
2. The 'leadership skill' measures whether the manager can manage and coordinate his subordinates sophisticatedly.
3. The 'business knowledge' measures whether the manager processes rich general knowledge to solve business problems.
4. The 'analytical and judicious ability' measures whether the manager can analyse the market conditions and business environment with constructive recommendation to the right person at the right time in the right place.
5. The 'training skill' measures whether the manager can provide a systematic approach to train and develop his subordinates.

6. The 'external relationship' measures whether the manager can process good relationship with the external parties and maintain a win-win approach for all parties concerned (i.e. the bank and the client both can gain the best.)
7. The 'innovative ability' measures whether the manager possesses ability to recommend new idea in response to the new challenge.
8. The 'sense of responsibility' measures the manager's self-initiative with respect to his business scope.
9. The 'personal conduct and behaviour' measures the manager's loyalty to the country and the Bank as well.
10. The 'interpersonal relationship' measures whether the manager possesses the ability of being well respected by his colleagues.

Appendix 7

The Current Operation Structure

1. Deposit-taking operations

- a. Provide information to customers about the deposit products available and the term structure (eg. interest rate, exchange rate, maturity period).
- b. Assist customers in determining the deposit products.
- c. Attract more deposits with the lowest cost (eg. current deposit and Hong Kong dollar saving deposit are two examples of low cost deposits.)
- d. Attract different categories of depositors to provide different sources of deposit eg. commercial depositors provide current deposit, overseas Chinese provide long term stable deposit.
- e. Monitor the preference of depositors and provide such information for strategic planning departments for reference.

- f. Educate depositors to use of depository mechanisms such as automated teller machines, telephone banking, mail banking in order to improve the depository operations efficiency.
- g. Market new deposit products to customers. For the first three points, the branch has to cooperate with the Treasury department to obtain the best interest rate, exchange rate for the customer. Otherwise for general depositors, a standard deposit rate will be offered. Subject to the system control, a branch manager has limited discretionary power to grant privileged interest rate (ie. better than the standard rate.)
- h. For the last four points, the branch has to closely cooperate with the Retail Banking Planning Department to develop the operation procedures and marketing strategy.

2. Loans Operations

- a. Market the loans products to the right customers.
- b. Assist customers' in selecting the loan portfolio that will best suit the needs of them.
- c. Perform the preliminary credit review and determine the amount and type of security required

from customers for charging.

- d. Offer the loans term and interest rate to the customers according to the results of previous analysis.
- e. Receive the completed application forms from the customers.
- f. If the loan amount is within the branch manager authority, the loan will be decided at Branch level. Otherwise, the application will be further reviewed by the Loan Department for approval.
- g. All the legal documents and loans documents are processed by the Loans Department because the branch does not have the necessary expertise.
- h. Annual review of the customer's credit standing and decide whether the terms and pricing have to be changed or not.
- i. Take remedial actions on problem loan
- j. Reflect the market and environmental (eg. trading cycle) change to the strategic planning department to assist the planner to amend/develop the strategy.

- k. For bills (documentary credits) transactions, the operations procedures are centralized in the bills center so that there is no need to place any technical staff in the branch to deal with these transactions.
- l. For the first four points, the branch has to closely cooperated with the Branch Administration Department and the Credit and Loans Planning Department especially for the monitoring and pricing of special customers (eg. the top ten loan customers in the branch.)
- m. For those credit review procedures, documentary routines, and legal procedures are all monitored by the Loans Department. Therefore a mutual communication between the branch and the Loans Department is very often in practice.
- n. Refer some special loans such as syndicated loans, leverage leasing, and loan booking to the Merchant Banking Department.

3. Agency Businesses

- a. Make use of other banking business for their retail business outlets.

- b. Credit Card business is a typical product to employ branches to extend its business to the bank's customers eg. promotion by granting a card free of first year annual charge to a mortgage loan customer.
- c. Insurance business is another product to extend its business through branch's loans business eg. fire insurance with housing mortgage and shipping insurance with documentary credit.
- d. Acts on behalf other branches both from the same bank or other member banks for current and saving accounts withdrawal or deposit-taking, and bullion trading.

4. Administrative Operations

- a. A lot of back office departments supporting the branch operations.
- b. Beyond those direct supporting departments such as the Credit and Loans Planning Department, there are three major back offices provide the key administrative support:
 - i. Personnel Department: responsible for the recruitment, promotion, and training of the branches's staff.

- ii. General Affairs : responsible for the
Department acquisition of branch's
equipment, furniture
and fixture. Instal-
lation of safety and
burglar alarming de-
vices.

- iii. Financial Control : responsible for the
Division development and running
of the branch's ac-
counting system, re-
porting system, manage-
ment accounting system
and maintenance of
personal computers.

BIBLIOGRAPHY

Books

- Bennett, S. G. and Paratt, K. J. Elements of Personnel Management. U.K.: Gee & Co. (Publishers) Ltd., 1979.
- Berkun, Toby, etc. Branch Management. U.S.A.: The Institute of Financial Education, 1987.
- Capron, H. L. Computers : Tools for an Information Age. U.S.A.: The Benjamin/Cummings Publishing Company Inc., 1987.
- Chadwick, Leslie and Magin, Michael. Creative Cost and Management Accounting. Hutuchinson Education, 1989.
- Cole, Leonard P. Cost Analysis and Controls in Banks. U.S.A.: Bankers Publishing Company, 1985.
- Davis, Gordon B. and Olson, Margrethe H. Management Information Systems. 2nd ed. New York : McGraw-Hill Book Company.
- Davis, Steven I. Excellence in Banking. 2nd ed. U.S.A.: Macmillan Press, 1986.

Eison, Charles L. and Ray, Charles M. Supervision. New York:
The Dryden Press, 1983.

Giardini, Valerie. Internal Transfer Pricing of Bank Funds.
U.S.A.: Bank Administration Institute, 1983.

Hellriegel & Slocum. Management. 4th ed. U.S.A.: Addison
Wesley, 1986.

Horngren, Charles T. Cost Accounting : A Managerial Emphasis.
5th ed. Englewood Cliffs, N. J.: Prentice-Hall, Inc.

Lucey, T. Management Information Systems. 5th ed. U.K. : ELBS

Novit, Mitchell S. Essential of Personnel Management.
Englewood Cliffs, N. J.: Prentice-Hall, Inc., 1979.

Otley, David. Accounting Control and Organisational Behaviour.
U.K.:The Chartered Institute of Management Accountants,1987.

Ramanauskas-Marconi, Helene. Behavioral Accounting. U.S.A.:
South-Western Publishing Co., 1989.

Thomason, George. A Textbook of Personnel Management. 4th ed.
U.K.: Institute of Personnel Management, 1981.

Periodicals

- "Overhead Cost Allocation in Service Organisations." Management Accounting (U.K.), June 1990, pp.36-37.
- "Bank of China Group and Hong Kong and Macao's Economy Prosper Simultaneously." Studies of International Finance (Beijing), May 1990, p.17.
- "Analysis the Development, Role and Direction of Bank of China Group in Hong Kong." Studies of International Finance (Beijing), May 1990, p.19.
- "Increasing Productivity : Performance Appraisal and Reward Systems." Personnel Review 19 (No.2 1990).
- "Evaluating Employees by Computer." Personnel Administrator, Nov. 1989.
- "Improve Performance by Appraisal." Human Resource Magazine on Human Resource Management, July 1990.
- Annual Report, Commissioner of Banking (H.K.), 1989.

CUHK Libraries



000321114